FILED

96 831 NOV 25 1996

OFFICE OF THE CLERK

No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1996

EDMUND M. MAHERN, TRUSTEE FOR MERCHANTS GRAIN, INC.,
Petitioner,

v.

MARK AND CHRIS ADKINS, *et al.*,
Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

---

PETITION FOR A WRIT OF CERTIORARI

JAMES M. CARR
JOSEPH H. YEAGER, JR.*
BAKER & DANIELS
300 North Meridian Street
Suite 2700
Indianapolis, IN 46204
(317) 237-0300
Counsel for Petitioner
* Counsel of Record

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

81 pp

QUESTIONS PRESENTED

Does Bankruptcy Code § 545 bar enforcement in bankruptcy of a state-created unperfected lien in favor of an entire class of creditors in that state, to the detriment of identically-situated creditors of the same debtor in other states?

A. Does this Court's decision in *Farrey v. Sanderfoot*, 500 U.S. 291 (1991), which relates to 11 U.S.C. § 522(f), limit the avoiding powers granted to a trustee by Bankruptcy Code § 545 so that a trustee may avoid only those statutory liens that attach after the debtor acquired the property in question?

B. Does property that is subject to a lien or security interest nonetheless become property of the bankruptcy estate created when the owner of that property files a petition under the Bankruptcy Code?

LIST OF ALL PARTIES

Pursuant to S.Ct. Rule 14.1(b), Petitioner supplies the list of all parties at Appendix, p. 48a-50a.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
LIST OF ALL PARTIES	ii
TABLE OF AUTHORITIES	v
CITATIONS TO OPINIONS BELOW	1
JURISDICTIONAL STATEMENT	1
STATUTORY PROVISIONS INVOLVED	1
STATEMENT OF THE CASE	2
REASONS FOR GRANTING THE PETITION	5
Summary And Introduction	5
I. THE SEVENTH CIRCUIT'S HOLDING THAT 11 U.S.C. § 545 CANNOT BE USED TO AVOID LIENS THAT ENCUMBER PROPERTY AT THE TIME OF THE DEBTOR'S ACQUISITION INCORRECTLY DECIDES AN IMPORTANT FEDERAL ISSUE AND CONFLICTS WITH THE DECISIONS OF OTHER CIRCUITS	7
A. As The Seventh Circuit Acknowledged, Its Decision Conflicts With The Decisions Of Other Circuits	9
B. The Questions Presented Involve Important Federal Issues, As the Seventh Circuit's Decision Directly Undercuts One Of The Two Fundamental Congressional Policies On Bankruptcy: Equality Of Distribution Across State Lines	13
C. The Seventh Circuit's Decision Should Be Reversed	15

TABLE OF CONTENTS—Continued

Page

II. THE SEVENTH CIRCUIT'S STATEMENT THAT THE GRAIN WAS NOT AN INTEREST OF THE DEBTOR IN PROPERTY CONTRADICTS ALL PRIOR LAW ON THE SUBJECT.. 20

A. The Seventh Circuit's Opinion States That Property Subject To A Lien Is Not Property Of The Estate, Contradicting A Prior Decision Of This Court 20

B. This Issue Is Important; If the Seventh Circuit's Statements Were To Be Left Undisturbed, A Fundamental and Long-Standing Feature Of Bankruptcy Law Will Be Undermined 21

CONCLUSION 22

TABLE OF AUTHORITIES

Cases	Page
Atlantic Cleaners & Dyers v. United States, 286 U.S. 427 (1932)	15
Begier v. Internal Revenue Service, 496 U.S. 53 (1990)	13
Christison v. United States, 960 F.2d 613 (7th Cir. 1992)	12
Dominion Bank of Cumberlands, NA v. Nuckolls, 780 F.2d 408 (4th Cir. 1985)	16
Farrey v. Sanderfoot, 500 U.S. 291 (1991)	*passim*
Graffen v. City of Philadelphia, 984 F.2d 91 (3d Cir. 1992)	12
In re Bates, 148 B.R. 541 (Bankr. N.D. Ill. 1993), *aff'd* 161 B.R. 965 (N.D. Ill. 1993)	8
In re DeLiguori, 146 B.R. 52 (Bankr. D.N.H. 1992)	8
In re Garcia, 149 B.R. 530 (Bankr. N.D. Ill. 1993), *aff'd* 155 B.R. 173 (N.D. Ill. 1993)	8
In re Hall, 752 F.2d 582 (11th Cir. 1985)	16
In re Hudgins, 967 F.2d 973 (4th Cir. 1992)	12
In re Kachina Publications, Inc., 171 B.R. 671 (Bankr. D. Ariz. 1994)	13
In re LMS Holding Co., 50 F.3d 1526 (10th Cir. 1995)	7, 9, 10, 12
In re Loretto Winery Ltd., 898 F.2d 715 (9th Cir. 1990)	7, 10-12
In re Merchants Grain, Inc., 93 F.3d 1347 (7th Cir. 1996)	1, 4
In re Misco Supply Co., 43 B.R. 651 (Bankr. D. Kan. 1984)	11
In re O'Connell, 167 B.R. 928 (Bankr. D. Mont. 1994)	8
In re Parrish, 144 B.R. 349 (Bankr. W.D. Tex. 1992)	9
In re Pierce, 809 F.2d 1356 (8th Cir. 1987)	11
In re Sanderfoot, 899 F.2d 598 (7th Cir. 1990), *rev'd sub nom. Farrey v. Sanderfoot*, 500 U.S. 291 (1991)	8
In re Stanford, 826 F.2d 353 (5th Cir. 1987)	13

TABLE OF AUTHORITIES—Continued

Page

In re Walter, 45 F.3d 1023 (6th Cir. 1995) 7, 10-13
In re Wilkinson, 196 B.R. 311 (Bankr. E.D. Va. 1996) 8
In re Woods Farmers Coop. Elevator Co., 946 F.2d 1411 (8th Cir. 1991) 7, 9-12
Internal Revenue Service v. Diperna, 195 B.R. 358 (E.D.N.C. 1996) 13
Maryland Nat'l Bank v. Mayor of Baltimore, 723 F.2d 1138 (4th Cir. 1983) 22
Merchants Grain, Inc. v. Adkins, 184 B.R. 52 (S.D. Ind. 1995) 1, 4
Naqvi v. Fisher, 192 B.R. 591 (D.N.H. 1995) 8
Ohio v. Kovacs, 469 U.S. 274 (1985) 12
Ohio Agric. Commodity Fund v. Mahern, 116 S. Ct. 1411, 134 L.Ed.2d 537 (1996) 5
Oregon Waste Systems, Inc. v. Department of Envtl. Quality, 511 U.S. 93 (1994) 14
Seminole Tribe of Florida v. Florida, 116 S. Ct. 1114, 134 L.Ed.2d 252 (1996) 5
Union Bank v. Wolas, 502 U.S. 151 (1991) 13
United States Nat'l Bank v. Chase Nat'l Bank, 331 U.S. 28 (1947) 22
United States v. Whiting Pools, Inc., 462 U.S. 198 (1983) 12, 20, 21

Constitution, Statutes and Rules

U.S. Const. art. 1, § 8, cl. 4 13
11 U.S.C. § 362 21
11 U.S.C. § 522 ..... *passim*
11 U.S.C. § 541(a) 20
11 U.S.C. § 545 ..... *passim*
11 U.S.C. § 547 3
28 U.S.C. § 1254(1) 1
Bankrtupcy Act § 67(b,c) 14
Chandler Act, Act of June 22, 1938, Ch. 575, 52 Stat. 840 (1938) 6
Ohio Rev. Code § 926.021(A) 20
Ohio Rev. Code § 926.021(C) 20

TABLE OF AUTHORITIES—Continued

	Page
S.Ct. Rule 14.1(b)	1
S.Ct. Rule 14.1(d)	1
Miscellaneous	
4 Collier on Bankruptcy ¶ 545.03 [1] (15th ed. 1996)	13
American Heritage Dictionary of the English Language 477 (1975)	19
Black's Law Dictionary 637 (6th ed. 1990)	19
C. Robert Morris, "Bankrupt Fantasy: The Site of Missing Words and the Order of Illusory Events," 45 Ark. L. Rev. 265 (1992)	9, 15
H.R. Rep. No. 595, 95th Cong., 2d Sess., 126-27 (1978), *reprinted in* 1978 U.S.C.C.A.N. 6087-88	16-17
H.R. Rep. No. 595, 95th Cong., 2d Sess., 362 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6318	12
John J. McCoid II, "Statutory Liens in Bankruptcy," 68 Amer. Bankr.J. 269 (1994)	13
Lawrence Kalevitch, "Sctoff and Bankruptcy," 41 Cleve. St. L.Rev. 599, 671 (1993)	9
S. Rep. No. 989, 95th Cong., 2d Sess., 76 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5862	16
Thomas G. Kelch, "An Apology For Plain-Meaning Interpretation of the Bankruptcy Code," 10 Bankr. Dev. J. 289 (1994)	9
Webster's New International Dictionary 921 (2d ed. 1954) *unabridged*	19

PETITION FOR A WRIT OF CERTIORARI

CITATIONS TO OPINIONS BELOW

Pursuant to S.Ct. Rule 14.1(d), Petitioner submits the following citations of the official and unofficial reports of the opinions and orders entered in this case below:

Merchants Grain, Inc. v. Adkins, 184 B.R. 52 (S.D. Ind. 1995);

In re Merchants Grain, Inc., 93 F.3d 1347 (7th Cir. 1996).

JURISDICTIONAL STATEMENT

This is a petition for certiorari with regard to a decision of the United States Court of Appeals for the Seventh Circuit entered on August 27, 1996. No party has sought rehearing or any extension of time to file this petition. This Court has jurisdiction of this petition pursuant to 28 U.S.C. § 1254(1) and S. Ct. Rule 10(a) and 10(c).

STATUTORY PROVISIONS INVOLVED

Pursuant to S.Ct. Rule 14.1(f), petitioner hereby sets out in full the text of 11 U.S.C. § 545:

§ 545. Statutory liens

The trustee may avoid the fixing of a statutory lien on property of the debtor to the extent that such lien—

(1) first becomes effective against the debtor—

(A) when a case under this title concerning the debtor is commenced;

(B) when an insolvency proceeding other than under this title concerning the debtor is commenced;

(C) when a custodian is appointed or authorized to take or takes possession;

(D) when the debtor becomes insolvent;

(E) when the debtor's financial condition fails to meet a specified standard; or

(F) at the time of an execution against property of the debtor levied at the instance of an entity other than the holder of such statutory lien;

(2) is not perfected or enforceable at the time of the commencement of the case against a bona fide purchaser that purchases such property at the time of the commencement of the case, whether or not such a purchaser exists;

(3) is for rent; or

(4) is a lien of distress for rent.

STATEMENT OF THE CASE

In 1990, Merchants Grain, Inc. ("MGI") owned and operated grain elevators in several states, including Indiana, Kentucky, Tennessee and Ohio. MGI often bought grain from farmers under so-called delayed pricing ("DP") contracts, under which farmers delivered grain to MGI and title passed to MGI. Payment from MGI to the farmers was deferred for up to twelve months so that the farmers could watch the grain markets rise and fall, selecting the best time to price the grain and demand payment. The DP contracts specified that the farmer/seller would remain "a common creditor" for the purchase price of the grain. App. at 2a.

In the fall of 1990 the Ohio Department of Agriculture learned that MGI was in financial difficulty. *Id.* at 3a. However, instead of using their statutory powers to shut down MGI's Columbus elevator, the Ohio regulators allowed MGI to continue to operate through the 1990 harvest. *Id.* at 3a. The Ohio regulators demanded that MGI agree that grain delivered to MGI's Columbus elevator be used to pay Ohio farmers. *Id.* at 3a-4a.

Neither federal regulators nor those in other states took any action with regard to MGI during that harvest.

MGI's cash flow dwindled after the harvest of 1990. *Id.* at 4a. Nonetheless, because of the actions of the Ohio regulators the defendants in this case (the "Ohio Farmers") were being paid, while by January 1991 many of MGI's checks to farmers in other states were being dishonored. As a result, all the Ohio Farmers were paid in full for grain sold under DP contracts, while hundreds of farmers in Indiana, Kentucky and Tennessee were left holding largely uncollectible unsecured claims totalling as much as nine million dollars.

An Indiana state court placed MGI in receivership in April, 1991 appointing as receiver Edmund Mahern. On May 9, 1991, receiver Mahern filed a petition for MGI under Chapter 11 of the United States Bankruptcy Code. *Id.* at 5a. The bankruptcy court later appointed Mahern Trustee and converted the case to one under Chapter 7. After Mahern (the "Trustee") learned of the nearly $3 million in payments to Ohio Farmers during the 90 days preceding MGI's bankruptcy petition, he commenced this action to recover those payments as preferences under Bankruptcy Code § 547. The Ohio Agricultural Commodity Depositors Fund (the "Fund") intervened in this action on the grounds that it would ultimately be required to reimburse "most" Ohio farmers for any judgment the Trustee achieves in this case. "Motion For Leave to Intervene In Adversary Proceedings . . .", filed by the Fund in the bankruptcy court on April 15, 1993.

The Fund and the Ohio Farmers raised a variety of defenses, on which they sought summary judgment. One defense was the assertion that the Farmers were secured creditors under an Ohio statute, and so immune from preference recovery. Neither the Ohio Farmers nor the Fund disputed the Trustee's contention that the question of whether the Farmers held unavoidable statutory liens making them secured creditors turned upon § 545 of the Bank-

ruptcy Code. The Bankruptcy Court granted the Ohio Farmers' and the Fund's summary judgment motions. App. at 35a-47a.

The Trustee appealed to the United States District Court for the Southern District of Indiana, which affirmed on the bases that the Ohio Farmers were protected by an Ohio statutory lien that the Trustee could not have avoided, and that the Ohio Farmers' grain, being subject to their lien, never became property of MGI's estate even after sold to MGI. *Merchants Grain, Inc. v. Adkins,* 184 B.R. 52 (S.D. Ind. 1995); App. at 22a-34a. Neither the parties nor the court questioned that § 545 governed the lien avoidance issue.

The Trustee then appealed to the United States Court of Appeals for the Seventh Circuit. He argued that the Ohio statutory lien was avoidable under § 545(1) because it became effective on MGI's insolvency, and that the lien was also avoidable under § 545(2) because it would not be enforceable against a bona fide purchaser. The Trustee also offered the Seventh Circuit well-established authority rebutting the suggestion that property subject to a lien does not become property of a bankruptcy estate.

The Seventh Circuit ruled on August 27, 1996, affirming the District Court, but on grounds not relied upon by either the bankruptcy court or the district court, grounds never argued or raised by any party. *In re Merchants Grain, Inc.*, 93 F.3d 1347 (7th Cir. 1996); App. at 1a-21a. First, the Seventh Circuit interpreted the Ohio statute to provide that the lien became effective on delivery of the grain to MGI. Second, it held that because the grain deposits were encumbered when MGI received them, they "were never 'an interest of the debtor in property.'" App. at 16a. Third, the Seventh Circuit relied on this Court's analysis of similar language in § 522(f) in *Farrey v. Sanderfoot,* 500 U.S. 291 (1991) to hold that § 545

did not control this case because the lien in question did not postdate the debtor's acquisition of the underlying property—the grain.

The court acknowledged that its analysis deviated from precedent:

> The trustee argues application of § 545, either (1) or (2), permits the avoidance of the Ohio liens. The trustee, the farmers, both courts below, and many other court decisions we have reviewed assume the relevance of this statute to avoiding liens. We cannot agree.

App. at 17a (footnote omitted).

The Seventh Circuit's decision was the first suggestion in this case that § 545 would not control the lien avoidance issue. To the contrary, the Fund and the Ohio Farmers have consistently argued that § 545 applied but provided no avoidance power under these facts.[1]

REASONS FOR GRANTING THE PETITION

Summary And Introduction

In this case the Seventh Circuit acknowledged that it was disagreeing with the views of at least four other circuits as to the application of 11 U.S.C. § 545. The Seventh Circuit's holding that an Ohio statutory grain

---

[1] The Trustee had first sued not the Ohio Farmers but instead the Ohio Agricultural Commodity Depositors Fund, as the beneficiary of the preferential transfers. Only after his case against the Fund (the "Fund Case") was dismissed under the Eleventh Amendment did Mahern bring this action directly against the Ohio Farmers. This Court granted *certiorari*, vacated, and remanded to the Seventh Circuit for further consideration in light of *Seminole Tribe of Florida v. Florida*, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996). *Ohio Agric. Commodity Fund v. Mahern*, 116 S. Ct. 1411, 134 L.Ed.2d 537 (1996).

depositors' lien could not be avoided under § 545 ratified the preferential treatment of 172 Ohio farmer/creditors over several hundred identically situated farmer/creditors located in Indiana, Kentucky and Tennessee. This result raises important issues of federal law upon which this Court should rule including: Does this Court's decision in *Farrey v. Sanderfoot*, 500 U.S. 291 (1991), which relates to 11 U.S.C. § 522(f), limit the avoiding powers granted to a trustee by 11 U.S.C. § 545 so that a trustee may avoid only those statutory liens that attached after the debtor acquired the property in question?

The Seventh Circuit's opinion grants to states, for the first time since the passage of the Chandler Act in 1938, the power to create broad priorities favoring their own citizens and enforceable in bankruptcy. Act of June 22, 1938, Ch. 575, 52 Stat. 840 (1938). It undermines the careful balance between federal and state interests achieved over the nearly 60 years since the Chandler Act, during which time Congress has consistently acted to enforce a uniform system of national bankruptcy distribution. Letting this opinion stand would provide states a roadmap for legislation to create state priorities enforceable in bankruptcy, not only for their grain depositors but for a broad variety of sellers, growers and manufacturers. This result undermines the strong Congressional policy of uniform bankruptcy distribution across state lines.

The Seventh Circuit reached this result by two specific but erroneous holdings. First, contrary to prior rulings of this Court and other Circuits, the Seventh Circuit stated that a debtor's property that is subject to a lien is not property of a bankruptcy estate. Left standing, this ruling would fundamentally change bankruptcy law, again without Congressional input, and render moot several provisions of the Bankruptcy Code. Second, the Seventh Circuit held that a trustee's avoidance power under 11 U.S.C. § 545 cannot be applied to avoid liens that attached at or before the time the debtor acquired the underlying

property. It expressly acknowledged that this holding deviated from the rulings of other Circuits as well as from those of the lower courts in this action. Even the Fund and the Ohio Farmers had implicitly conceded the applicability of § 545, having argued the case under § 545 themselves.

I. THE SEVENTH CIRCUIT'S HOLDING THAT 11 U.S.C. § 545 CANNOT BE USED TO AVOID LIENS THAT ENCUMBER PROPERTY AT THE TIME OF THE DEBTOR'S ACQUISITION INCORRECTLY DECIDES AN IMPORTANT FEDERAL ISSUE AND CONFLICTS WITH THE DECISIONS OF OTHER CIRCUITS.

The court below wrongly decided that a state could use a statutory producers' lien to provide farmers selling grain in that state a priority over identically-situated farmers selling grain to the same debtor in other states. It reached this conclusion by holding for the first time that 11 U.S.C. § 545 cannot be used to avoid any lien that attaches at the time the debtor receives title to the underlying property. This ruling decides an important federal question in a way that directly conflicts with the decisions of every other court that has decided the matter, including other circuit courts of appeal. *In re LMS Holding Co.*, 50 F.3d 1526, 1527 (10th Cir. 1995); *In re Walter*, 45 F.3d 1023, 1027 (6th Cir. 1995); *In re Loretto Winery Ltd.*, 898 F.2d 715, 717-18 (9th Cir. 1990); *In re Woods Farmers Coop. Elevator Co.*, 946 F.2d 1411, 1413 (8th Cir. 1991). Moreover, the decision validates a state-created priority scheme that undermines years of protective federal legislation.

The Seventh Circuit based this holding on *Farrey v. Sanderfoot*, 500 U.S. 291 (1991). *Farrey* interprets not Bankruptcy Code § 545 but instead Bankruptcy Code § 522(f). Section 552(f) protects a debtor's "fresh start" by allowing the debtor to avoid certain liens that would impair the debtor's exemptions. In *Farrey*, a state court

in a dissolution case awarded a husband the marital home. The state court contemporaneously imposed a judicial lien on the home to secure payments to the ex-wife. In what the dissent in the Seventh Circuit decision in *Farrey* would later call a "vicious scheme," the ex-husband then filed a bankruptcy petition and moved under § 522(f) to avoid the judicial lien securing the ex-wife's portion of the property division. *In re Sanderfoot*, 899 F.2d 598, 607 (7th Cir. 1990) (Possner, J., dissenting), *rev'd sub nom. Farrey v. Sanderfoot*, 500 U.S. 291 (1991).

This Court held that the ex-husband could not use § 522(f), which allowed avoidance of "the fixing of a lien on an interest of the debtor in property," to avoid his obligations to his ex-wife, where the "fixing" he sought to avoid did not post-date the debtor's acquisition of an interest in the property. *Farrey*, 500 U.S. at 295-301.

During the five years since *Farrey* was decided, the case law has limited *Farrey* largely to its own facts. No court has until now extended it beyond § 522(f) to § 545, with its wholly different purpose and different, if similar, language. Instead, lower courts have declined to expand *Farrey*'s rationale, more often distinguishing it. *See, e.g., In re Wilkinson*, 196 B.R. 311, 316-317 (Bankr. E.D. Va. 1996) (declines to apply *Farrey* to bar debtor from avoiding judgment lien attaching before payment of wages in question); *Naqvi v. Fisher*, 192 B.R. 591, 593 n.2 (D.N.H. 1995) ("complex issues identified and resolved in" *Farrey* not present); *In re O'Connell*, 167 B.R. 928, 929, 931 (Bankr. D. Mont. 1994) (declines to apply *Farrey* to motion to avoid attorney's lien); *In re Garcia*, 149 B.R. 530, 534 (Bankr. N.D. Ill. 1993) (distinguishes *Farrey* on the facts from avoidance of lien on unpaid wages), *aff'd*, 155 B.R. 173 (N.D. Ill. 1993); *In re Bates*, 148 B.R. 541, 548 (Bankr. N.D. Ill. 1993) (distinguishes *Farrey* in granting motion to avoid pre-existing judgment lien on wages to be paid), *aff'd*, 161 B.R. 965 (N.D. Ill. 1993); *In re DeLiguori*, 146 B.R. 52, 58 (Bankr. D.N.H.

1992) (distinguishing *Farrey*'s "unusual fact pattern"); *In re Parrish*, 144 B.R. 349, 353 (Bankr. W.D. Tex. 1992) (*Farrey* does not apply where one party brought property into marriage).[2]

At the same time, courts have continued to interpret § 545 as they did before, applying it to liens regardless of when they attached. *See, e.g., In re LMS Holding Co.*, 50 F.3d 1526 (10th Cir. 1995); *In re Woods Farmers Coop. Elevator Co.*, 946 F.2d 1411 (8th Cir. 1991). That has now changed, with the Seventh Circuit expanding *Farrey* far beyond its facts and its legal context to reach a conclusion that this Court should carefully examine.

A. As The Seventh Circuit Acknowledged, Its Decision Conflicts With The Decisions Of Other Circuits.

The Seventh Circuit veered from the analysis of all the parties and both lower courts in this case. Citing *Farrey*, it recast § 545's grant of authority, narrowing that avoidance power by immunizing from it any liens attaching to property at or before the time the debtor acquired the property. App. at 17a-18a. Combining this newly-created limitation of § 545 with the conclusion that the Ohio statutory lien attached at the time the Ohio Farmers delivered their grain, the court concluded § 545 cannot be applied in this case. *Id.* at 18a-19a. The court reasoned that when the lien "fixed" to the grain the grain was not property of the debtor. *Id.*

---

[2] *Farrey*'s reasoning has also been criticized by commentators. *See, e.g.*, C. Robert Morris, "Bankrupt Fantasy: The Site of Missing Words and the Order of Illusory Events," 45 Ark. L.Rev. 265, 287-294 (1992) (disagreeing with *Farrey*'s analysis); Thomas G. Kelch, "An Apology For Plain-Meaning Interpretation of the Bankruptcy Code," 10 Bankr. Dev. J. 289, 308 (1994) (*Farrey* and *Owen v. Owen*, 500 U.S. 305 (1991), have "been the subject of much derisive comment."); Lawrence Kalevitch, "Setoff and Bankruptcy," 41 Cleve. St. L.Rev. 599, 671 (1993) (*Farrey* is "generally unhelpful").

In the passage quoted above at page 5, the Seventh Circuit expressly acknowledged the split between its analysis and that of at least four other circuits. "We cannot agree" with the decisions of other circuits applying § 545 to avoiding liens. *Id.* at 17a (footnote omitted). The four circuits were the Sixth, Eighth, Ninth and Tenth.[a]

The Seventh Circuit was correct that those four cases are examples of the many cases that have applied § 545 to lien avoidance. The distinction the court made—between avoiding a lien and avoiding the fixing of a lien—is by itself of little legal consequence. However, the court went on (following *Farrey*) narrowly to construe "fixing" as limited to attachment of liens to property already owned by the debtor. With that, the court for the first time held that § 545 cannot apply to avoid any lien that encumbered property at the time the debtor acquired it. That holding creates the real conflict here, both with other circuits and with the congressional policy of uniform distribution.

The four cases cited by the court illustrate the nature, but not the full extent, of the conflict raised by the Seventh Circuit's decision. First, in *In re LMS Holding Co.*, 50 F.3d 1526 (10th Cir. 1995), the Tenth Circuit used § 545 to analyze the avoidance of a statutory lien. *Id.* at 1527. There the lien, held by the IRS, had attached to the property before the debtor acquired the property. *See id.* Although the Tenth Circuit ultimately concluded, under § 545(2), that the lien was not avoidable because

---

[a] The footnote read: "*See, e.g., In re Walter*, 45 F.3d 1023, 1027 (6th Cir. 1995) ('Section 545 of the Bankruptcy Code dictates when a trustee can avoid statutory liens.'); *In re Loretto Winery Ltd.*, 898 F.2d 715, 717-18 (9th Cir. 1990) ('Section 545 of the Bankruptcy Code, 11 U.S.C. § 545, dictates when a trustee can avoid a statutory lien.'); *In re Woods Farmers Cooperative Elevator Co.*, 946 F.2d 1411, 1413 (8th Cir. 1991) ('[Section 545 of the] Bankruptcy Code allows the bankruptcy trustee to avoid certain statutory liens.'); *In re LMS Holding Co.*, 50 F.3d 1526, 1527 (10th Cir. 1995) (analyzing § 545(2) as a lien avoidance provision)."

a bona fide purchaser could not defeat it, under the Seventh Circuit's analysis § 545 would never have come into play.

Second, *In re Woods Farmers Coop. Elevator Co.*, 946 F.2d 1411 (8th Cir. 1991) dealt with a North Dakota producers lien which, like the lien here, attached at the time of sale to protect sellers of commodities. *Id.* at 1413. The bankruptcy court avoided the lien under § 545(2). *See id.* The district court reversed, still under § 545(2), on the analysis that under North Dakota law a bona fide purchaser could not defeat the lien. *Id.* The Eighth Circuit, still applying § 545(2), agreed with the district court. *Id.* at 1414. Under the Seventh Circuit's analysis, however, § 545 would never have been applied.

Third, in *In re Loretto Winery Ltd.*, 898 F.2d 715 (9th Cir. 1995), a bankruptcy court avoided a producers lien under § 545. *See id.* at 717. The bankruptcy appellate panel affirmed. The Ninth Circuit reversed, but not because it thought § 545 did not apply. Instead, like every other court that has visited the subject until now, the Ninth Circuit analyzed the case under § 545 even though the lien attached at delivery of the goods. *See id.* at 717-725.

Other courts have also crossed the line the Seventh Circuit now draws, applying § 545 even where the lien in question did not post-date the debtor's acquisition of the property. *In re Pierce*, 809 F.2d 1356, 1359 (8th Cir. 1987) (court used § 545 to analyze attempt to avoid statutory attorney's lien on proceeds where lien attached to underlying cause of action); *In re Misco Supply Co.*, 43 B.R. 651, 652-53 (Bankr. D. Kan. 1984) (Louisiana statutory vendor's lien, attaching at sale, analyzed under § 545).

The fourth case the Seventh Circuit cited as contrary, *In re Walter*, 45 F.3d 1023 (6th Cir. 1995), deviates from the Seventh Circuit's later analysis by referring to avoiding a "lien" rather than the "fixing of a lien." *Id.*

at 1027. However, in contrast to *LMS*, *Loretto Winery*, and *Woods*, the lien in *Walter* did post-date the debtor's acquisition of the property. The *Walter* court read no extra conditions into § 545:

> Pursuant to this section, a trustee may step into the shoes of a hypothetical bona fide purchaser and claim the same defenses to statutory liens on a debtor's property as would a bona fide purchaser.

Id.

The Seventh Circuit cited *Walter* as a case that assumed that § 545 works to avoid liens, rather than avoiding the fixing of liens. As discussed at page 10 above, that distinction becomes important only in light of the *Farrey* court's narrow construction of the term "fixing" as limited to attachment of a lien after title to the underlying property passed to the debtor.

Congress itself, in discussing § 522, apparently placed far less importance on this distinction than did the Seventh Circuit. "Subsection (f) protects the debtor's exemptions, his discharge, and thus his fresh start by permitting him to *avoid certain liens* on exempt property." H.R. Rep. No. 595, 95th Cong., 2d Sess., 362 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6318 (emphasis supplied). Moreover, many other courts, including this Court, have both before and since *Farrey* routinely used the same terminology (§ 545 as avoiding liens rather than the fixing of liens) without any reaction from Congress.[4]

---

[4] *See, e.g., Ohio v. Kovacs*, 469 U.S. 274, 286 (1985) (O'Connor, J., concurring) (under § 545, "trustee may avoid statutory liens only in specified circumstances"); *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 208 n.15 (1983) (under § 545, "trustee has power to avoid statutory liens"); *Graffen v. City of Philadelphia*, 984 F.2d 91, 94 (3d Cir. 1992) (analyzes § 545 as a lien avoidance provision); *In re Hudgins*, 967 F.2d 973, 975 (4th Cir. 1992) ("bankruptcy trustee may avoid a statutory lien" under § 545, were not enforceable against the bona fide purchaser); *Christison v. United States*, 960 F.2d 613, 614 (7th Cir. 1992) (under § 545, "a trustee may avoid a statutory lien not enforceable at the commencement

None of these cases applies *Farrey* or its analysis to § 545.

B. The Questions Presented Involve Important Federal Issues, As the Seventh Circuit's Decision Directly Undercuts One Of The Two Fundamental Congressional Policies On Bankruptcy: Equality Of Distribution Across State Lines.

As this Court has observed, "Equality of distribution among creditors is a central policy of the Bankruptcy Code." *Begier v. Internal Revenue Service*, 496 U.S. 53, 58 (1990). Congress and the Court have both consistently acted to preserve the uniformity of the national bankruptcy system contemplated by the Constitution, largely by striking down state efforts to give their own residents priority. *See, e.g., Union Bank v. Wolas*, 502 U.S. 151, 161 (1991) (cites legislative history for conclusion that equality of distribution is "prime bankruptcy policy"); U.S. Const. art. 1, § 8, cl. 4; John J. McCoid II, "Statutory Liens in Bankruptcy," 68 Amer. Bankr. J. 269, 276-286 (1994).

The Seventh Circuit's decision directly undercuts this policy, and in doing so undermines years of careful legislative balancing. Congress has legislated for over 50 years to prevent states from doing what Ohio did here: implement a state priority that will give those doing business in one state priority over identically-situated persons in other states. *Id.; see also,* 4 Collier on Bankruptcy ¶ 545.03 [1] (15th ed. 1996). As McCoid and Collier demon-

---

of the bankruptcy case against a bona fide purchaser"); *In re Stanford*, 826 F.2d 353, 355-357 (5th Cir. 1987) (in § 545 "Congress specifically provided the conditions under which statutory liens on a debtor's property could be avoided . . . ."); *Internal Revenue Service v. Diperna*, 195 B.R. 358, 360 (E.D.N.C. 1996) cites *Walter* for proposition that trustee has the same defenses to statutory liens as would a bona fide purchaser); *In re Kachina Publications, Inc.*, 171 B.R. 671, 672-673 (Bankr. D. Ariz. 1994) (debtor can use § 545 to avoid statutory lien if unperfected).

strate, Congress has acted through 11 U.S.C. § 545 and its Bankruptcy Act predecessor, § 67(b,c). As they have evolved over the years, those statutes have always been aimed at blocking the continuing efforts of states to create priorities to benefit their own residents and businesses who have claims against debtors in bankruptcy at the expense of similarly situated creditors in other states. *Id.*

If left standing, the Seventh Circuit's decision in this case will give states a blueprint to defeat this carefully crafted federal scheme. Simply by copying the Ohio statutory scheme, granting to sellers blanket unperfected liens against the assets of "failed" buyers, states will be able to exclude significant portions of their economies from the equal distribution provisions of the Bankruptcy Code. As states make and broaden producer-type lien statutes, favoring their own residents and businesses, they will undermine the constitutionally-contemplated and congressionally mandated goal of uniform distribution.

The Seventh Circuit erroneously dismissed the Trustee's argument based on these policies as challenges under the equal protection clause. The lower court cited an equal protection case, *Oregon Waste Systems, Inc. v. Department of Envtl. Quality*, 511 U.S. 93 (1994), for the proposition that the Ohio scheme "does not create any unconstitutional preference for one state's citizens at the expense of another's." App. at 20a-21a. However, the Trustee did not attack the Ohio scheme as violating the equal protection clause. Instead, he pointed out that the scheme undermined the strong constitutional and congressional policy in favor of uniform interstate distribution in bankruptcy, and against state preference schemes.

The issue of the meaning of a similar phrase, "fixing of a lien on an interest of the debtor in property," in § 522, was important enough to merit certiorari in *Farrey*. The issue carries even more import here, for the future of a uniform system of equal distribution as well as for the hundreds of Indiana, Kentucky and Tennessee farmers who

now bear more than their fair share of the loss from MGI's collapse.

C. The Seventh Circuit's Decision Should Be Reversed.

The Seventh Circuit rewrites § 545 to add a new element never before imposed under that section: that the lien sought to be avoided must have attached after the debtor acquired the property. As set forth above, no court before ever grafted such a requirement onto § 545. If Congress were dissatisfied with the courts' prior consistent interpretation of § 545, it would be for Congress, not the Seventh Circuit, to change the provision.

This Court did identify § 545(1) in a footnote as a relative of § 522(f) in which the word "fixing" referred to timing. *Farrey*, 500 U.S. at 296 n.3. Fairly read, that footnote does not by its context and should not by logic carry the *Farrey* analysis into § 545. At most it observes the undisputed fact that § 545(1) is time sensitive. "The word 'fixing' was not employed to emphasize a lien's temporal quality." Morris, *supra*, 45 Ark. L. Rev. at 290 (referring expressly to footnote 3 in *Farrey*).

The Seventh Circuit was wrong to apply this Court's construction of § 522(f) to §545 because the two sections of the Bankruptcy Code play wholly different roles in the federal bankruptcy scheme. The role of § 545 is not served (but instead undermined) by this construction, and the wording of the two sections of the Bankruptcy Code, while similar, is not identical.

1. *The Seventh Circuit Decision Undermines Strong Congressional Bankruptcy Policy.* The same statutory wording can and should be interpreted in different ways where necessary to give effect to the different provisions in which it appears. *Atlantic Cleaners & Dyers v. United States*, 286 U.S. 427, 433 (1932) ("It is not unusual for the same word to be used with different meanings in the same act, and there is no rule of statutory construction which precludes the courts from giving to the word the

meaning which the Legislature intended it should have in each instance.") Here, Sections 545 and 522(f) serve fundamentally different goals in the statutory scheme. Section 522(f) is a debtor-centered provision whereas § 545 is creditor-oriented. The express purpose of § 522 is to protect a debtor's "fresh start," one of the fundamental policies of bankruptcy law. As noted earlier, § 545 advances the other fundamental but independent policy of promoting equality of distribution to creditors.

Section 522 promotes a "fresh start" by protecting a debtor against overreaching creditors who, with the debtor in distress, may attempt to acquire broad judicial liens or blanket security interests that impair the debtor's fresh start. It functions to preserve assets for the debtor.

> The legislative history further reveals that Congress enacted section 522(f) as a response to what it viewed as unconscionable creditor practices in the consumer loan industry. H.R.Rep. No. 595, *supra*, at 126-27; 1978 U.S. Code Cong. & Ad.News, 6087-88. Congress evidenced its concern about overreaching creditors who obtained nonpossessory, *nonpurchase-money* security interests covering a substantial part of debtors' otherwise exempt property. Congress found that debtors usually granted blanket security interests, and agreed to waive their right to exempt property, without understanding the consequences of their actions.

In re Hall, 752 F.2d 582, 587-88 (11th Cir. 1985) (emphasis added); *see also Dominion Bank of Cumberlands, NA v. Nuckolls*, 780 F.2d 408, 413 (4th Cir. 1985); S. Rep. No. 989, 95th Cong., 2d Sess., 76 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5862. The legislative history shows Congress' intent to protect debtors in distress:

> The first right [§ 522(f)(1)] allows the debtor to undo the actions of creditors that bring legal action against the debtor shortly before bankruptcy. Bank-

> ruptcy exists to provide relief for the overburdened debtor. If a creditor beats the debtor into court, the debtor is nevertheless entitled to his exemptions.

H.R. Rep. No. 595, 95th Cong., 2d Sess., 126-27 (1978), *reprinted in* 1978 U.S.C.C.A.N. 6087-88. This Court itself, in *Farrey*, acknowledged "Congress intended § 522 (f)(1) to thwart a rush to the courthouse. . . ." *Farrey*, 500 U.S. at 298.

These authorities reflect that § 522(f)(1) is time sensitive. It is intended to preserve a debtor's fresh start by freeing his exempt property from the judicial liens of judgment creditors, and from the use by holders of blanket security interests of those interests as leverage to secure reaffirmation or other preferential treatment from a struggling debtor.

The *Farrey* limitation on the § 522 avoiding power would not keep a trustee from using § 522 as it was intended—to avoid these late-filed judicial liens against debtors in distress.

By contrast, § 545 serves a wholly different purpose in the bankruptcy system. As set forth above at pp. 13-16, § 545 is intended to protect the uniformity of a national bankruptcy system and equality of distribution by forbidding states from causing those who live and do business in one state to receive bankruptcy priority over persons from other states.

While limiting avoidance to late-attaching liens fits hand-in-glove with the policy of § 522(f), applying the same rule to § 545 would undercut the goal of § 545. It would not only allow, but indeed encourage, state-based priorities patterned after the Ohio grain producers' lien.

Moreover, the equities cut just as strongly in favor of avoidance here as they did against avoidance in *Farrey*. Expansion of the *Farrey* rule to govern this case would ratify the non-uniform and unfair result in which every Ohio farmer creditor of MGI was paid in full, based on state action and state law, while hundreds of otherwise

identically situated Indiana, Kentucky and Tennessee farmers lost millions of dollars.[6]

Based on these factors, under *Atlantic Cleaners*, the "fixing of a lien" language can and should be interpreted in § 545 differently from the way this Court interpreted that language in *Farrey*.

2. *The language of the two sections is different, eliminating any need for the two to be interpreted identically.* In addition to this fundamental policy difference between the sections, a heretofore overlooked difference in the language of the two statutes also supports different construction. Section 522 refers to the fixing of a lien "on an interest of the debtor in property", while § 545 refers merely to the fixing of a lien "on property of the debtor." This difference greatly mitigates the force of the rule of statutory construction supporting consistent interpretation of identical language—here the language is not identical. Instead, grammatical logic supports the distinction in application that good policy, as set above, commands.

An "interest" of the debtor in property arguably cannot exist before the debtor acquires the property. Since § 522 allows only avoidance of fixation on an "interest", under the *Farrey* analysis § 522(f) does not apply to liens attaching to other interests, before the debtor's acquisition created its interest. By contrast, "property" exists before, during and after its transfer from one party to another. Thus, a lien on property of a debtor did "fix" on that property, regardless of whether before or after the debtors' acquisition. And it is avoidance of fixation on "property" that § 545 allows.

---

[6] Moreover, as set forth in footnote one above, any judgment against the Ohio farmers in this case will ultimately be borne almost entirely by the state indemnity fund, not the farmers themselves. Thus what is sometimes seen as the harshness of a preference recovery would be mitigated here as the Fund, not the 172 farmer defendants, would bear the brunt of the recovery.

Thus it is entirely consistent with *Farrey* to distinguish between (one) § 522(f)'s avoidance of the fixing of a lien on "an interest of the debtor" that did not exist until the debtor got the property, and (two) § 545's avoidance of the fixing of a lien on "property" that, by contrast, did exist before the debtor acquired it.

Moreover, the *Farrey* Court's interpretation of "fixing" is not the only interpretation of that word. In a passage quoted verbatim by the Seventh Circuit, *Farrey* recited " 'fix' means 'to fasten a liability upon.' " *Farrey*, 500 U.S. at 296 (citing Black's Law Dictionary 637 (6th ed. 1990).[6] However, "fasten" is not limited to the meaning *Farrey* gives it—the attachment of a new object to an existing object. More generally "fasten" means to join things together, without presumption as to whether one preexisted the other. Webster's New International Dictionary 921 (2d ed. 1954) *unabridged* ("To cause to hold together *or* to something else.") (emphasis supplied); American Heritage Dictionary of the English Language 477 (1975) ("To attach to something else; join; connect"). None of these definitions require that one *res* preexist the other, let alone dictate which one must come first.

Accordingly, there is nothing inherent in the plain meaning of the verb "to fix" to limit it to the narrow meaning attributed to it in *Farrey*.

3. *The outcome of this case depends on this issue.* Whether the *Farrey* interpretation of § 522(f) should be transplanted into § 545 is outcome determinative. If § 545 is applied to this unperfected Ohio statutory lien, it will be avoided because a bona fide purchaser could have avoided the producers lien.[7] Indeed that is the only outcome that makes sense. The statute grants liens broadly,

---

[6] That definition actually reads "to fasten a liability upon one." *Id.*

[7] The Seventh Circuit never reached this issue. The District Court thought the lien, though unperfected, would be automatically perfected. Appendix at 34a.

to all "claimants" unable to procure payment for grain conveyed to an elevator. Ohio Rev. Code § 926.021(A). The lien covers essentially all the assets of a "failed" elevator (not just the grain). Ohio Rev. Code § 926.021(C). An elevator's day-to-day sales of large volumes of grain on the national and international markets would be seriously hindered, if not eliminated, if purchasers knew that their title was subject to the liens of every farmer who was yet to be paid by the elevator. Thus the transfers in satisfaction of the lien, challenged here as preferential, would be avoidable as they would have given the transferees more than they would have received as unsecured creditors in a hypothetical Chapter 7 case. The Seventh Circuit acknowledged the possibility of just this result. App. at 19a.

II. THE SEVENTH CIRCUIT'S STATEMENT THAT THE GRAIN WAS NOT AN INTEREST OF THE DEBTOR IN PROPERTY CONTRADICTS ALL PRIOR LAW ON THE SUBJECT.

The courts below, including the Seventh Circuit, wrongly stated that property of a debtor, subject to lien, is not "property of the estate." This important federal question was decided in a way that directly conflicts with the relevant decisions of this Court.

A. The Seventh Circuit's Opinion States That Property Subject To A Lien Is Not Property Of The Estate, Contradicting A Prior Decision Of This Court.

The Seventh Circuit's opinion states, and if left standing will be cited for, the proposition that property subject to a lien is not property of the estate. The District Court said the same thing. App. at 29a. This conflicts with the well-established construction of Bankruptcy Code § 541 (a), under which the estate consists of every interest of the debtor in property. As this Court held in *Whiting Pools*:

> Although Congress might have safeguarded the interests of secured creditors outright by excluding from

> the estate any property subject to a secured interest, it chose instead to include such property in the estate and to provide secured creditors with "adequate protection" for their interests.

Whiting Pools, 462 U.S. at 203-04.

B. This Issue Is Important; If the Seventh Circuit's Statements Were To Be Left Undisturbed, A Fundamental and Long-Standing Feature Of Bankruptcy Law Will Be Undermined.

This issue was important enough for this Court to address in *Whiting Pools*. The Court did so for good reason. The Seventh Circuit's view, as expressed in the opinion here under consideration, would mean trustees and debtors-in-possession will no longer have control of the debtor's property subject to liens. Under the Seventh Circuit's view, the automatic stay provided by Bankruptcy Code § 362 would no longer apply to acts against a debtor's property subject to security interests or other liens. Under the Seventh Circuit's view, motions for relief from stay under § 362 will no longer be necessary for secured creditors, since as set forth above the stay covers only property of the estate. Moreover, the concept of adequate protection for creditors' interests in their collateral would become meaningless, as debtors-in-possession or trustees will be deprived of their present ability to use the property subject to the provision to the creditor of adequate protection.

This rule would have the perverse effect of giving a secured creditor greater rights in bankruptcy than out of it. Under state law debtors retain title to collateral and the creditors must foreclose their liens and make a commercially reasonable disposition in order to realize on their collateral. Under the Seventh Circuit decision, the debtor's bankruptcy filing will ease the creditors' access to his collateral. "It is not . . . a bankruptcy objective to make a secured creditor better off than it would have been

had there been no bankruptcy at all." *Maryland Nat'l Bank* v. *Mayor of Baltimore*, 723 F.2d 1138, 1145 (4th Cir. 1983) (citing *United States Nat'l Bank v. Chase Nat'l Bank*, 331 U.S. 28 (1947)).

The change contemplated by the Seventh Circuit would also undermine both the fundamental policies of the Code, interfering with the debtor's fresh start by denying it use of liened property in a reorganization, and undercutting equality of distribution by tilting the existing balance sharply in favor of secured creditors and away from general creditors.

CONCLUSION

The Seventh Circuit's opinion contains two proclamations on bankruptcy law that will if left uncorrected leave serious dispute among the circuits on topics that affect many bankruptcy cases. These issues need the Court's attention so they can be resolved now before the Seventh Circuit's opinion begins to take hold to the detriment of policies Congress has taken years to refine and implement.

Respectfully submitted,

JAMES M. CARR
JOSEPH H. YEAGER, JR.*
BAKER & DANIELS
300 North Meridian Street
Suite 2700
Indianapolis, IN 46204
(317) 237-0300
Counsel for Petitioner

November 25, 1996

* Counsel of Record

APPENDICES

APPENDIX A

IN THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 95-2625

IN THE MATTER OF: MERCHANTS GRAIN, INCORPORATED, by and through receiver, EDMUND M. MAHERN,
Debtor.

Appeal of EDMUND M. MAHERN, Trustee
for Merchants Grain, Incorporated

Appeal from the United States District Court
for the Southern District of Indiana, Indianapolis Division.
No.95 C 30—Larry J. McKinney, *Judge*

ARGUED FEBRUARY 13, 1996—
DECIDED AUGUST 27, 1996

Before CUMMINGS, BAUER, and MANION, *Circuit Judges.*

MANION, *Circuit Judge.* The bankruptcy trustee for Merchants Grain, Inc. filed this action to recover payments made to farmers for the sale of their grain and to include these payments in the bankruptcy estate. The bankruptcy court and the district court ruled for the farmers. We affirm.

I.

Before it filed for bankruptcy on May 9, 1991, Merchants Grain, Inc. ("MGI") owned and operated grain storage and marketing facilities in six states, including one in Ohio. The Ohio facility located in Columbus, was a grain terminal facility providing both storage and transportation facilities. It had significantly more storage capacity than a typical grain elevator facility and was one of only two facilities of its capacity servicing central Ohio.

MGI offered several types of grain marketing contracts to farmers. In one of these, a delayed pricing contract, the farmer delivers grain to the elevator at harvest time but is not immediately paid for it. Instead, on a later date specified by the farmer, the elevator places the grain on the market and sells it at the going price. After subtracting the elevator operator's share, the proceeds from the sale are transferred to the farmer. Of couse an elevator operator cannot differentiate one farmer's grain from another's; the grain itself is fungible. The elevator simply owes the farmer for the quantity of grain deposited. The defendants in this case were all farmers who had delivered grain to MGI under a delayed pricing agreement.

Among other provisions, the delayed pricing agreement between MGI and grain depositors stipulated that title to the grain transferred to MGI upon delivery and that the depositor became a "common creditor" for the value of the grain. However, the contract alone did not define the entire relationship between MGI and the depositors at its Columbus, Ohio facility. State law also governed the grain transactions.

Ohio provides additional protection to farmers who market grain through Ohio grain elevators and terminals. Among those protections, Ohio law creates a statutory lien on the grain on behalf of the grain depositor. Ohio Rev. Code § 926.021. In addition, Ohio grants its De-

partment of Agriculture and its Director of Agriculture specific powers to regulate, license, and otherwise oversee the operations of grain storage and marketing facilities. Such facilities that are engaged in the business of agricultural product handling are referred to in the Ohio statutes as "agricultural commodities handlers." *See* Ohio Rev. Code § 926 *et seq.* (regulating agricultural commodity handlers). Included in its oversight authority the Director has the power to revoke, suspend, or conditionally suspend the license of an agricultural commodity handler that does not maintain statutorily sufficient assets to cover the outstanding receipts for grain deposits. Ohio requires agriculture commodities handlers to maintain a positive current net worth based on a formula involving the grain deposits over the preceding 12-month period. Ohio Rev. Code § 926.06(B).

As part of its oversight function, the Department of Agriculture reviewed MGI's financial statements, which in early September, 1990, revealed a negative current net worth of over $6,000,000. Rather than suspend MGI's license to operate its Ohio facility, the Department extended MGI several options for rectifying the violation. Although MGI and the Department exchanged correspondence over the next several months, MGI did not resolve its financial problem. The Department did not wish to suspend MGI's license because the fall grain harvest was under way and MGI's facility was vital to the central Ohio agricultural community. Without a facility to store grain for delayed pricing contracts, grain producers would be forced to cash-sale their grain at harvest time resulting in significantly lower prices and serious financial losses.

By November 8, 1990, MGI still had not complied with the statutory financial requirements and the Director of Agriculture conditionally suspended MGI's agriculture commodity handler's license pursuant to Ohio Rev. Code § 926.10. The conditional suspension restricted MGI's Columbus, Ohio operation but permitted the facility to

continue acquiring grain deposits. The Department required MGI to cover 100 percent of all grain obligations either with grain on hand or cash deposited in a segregated bank account located in Ohio. Between November and mid-December, the Department of Agriculture increased its oversight of MGI.

In late December, 1990, MGI issued a check to the federal government which was returned due to insufficient funds. When the Department was notified of this development, it immediately initiated a full examination of MGI's grain records and inventories. Before the Department completed its examination, MGI closed the Columbus facility, which at that time had close to one million bushels of grain on deposit.

On January 7, 1991, the Director fully suspended MGI's license. The Department of Agriculture and MGI thereafter reached a settlement agreement under which MGI was permitted to continue operating its Columbus facility under Department oversight of its day-to-day operations in order to sell the grain it had on deposit. The proceeds from the grain sales were deposited in one of three joint escrow accounts on which checks could be drawn only if they were signed by both the Department and MGI. While the agreement permitted MGI to sell the grain it had on deposit, it required MGI to consult with the Department regarding the sale price. The Department arranged for all grain depositors with delayed price contracts to accept payment terms providing the market price on the day of sale as their contract price. The Department verified the number of bushels credited to each depositor and the amount of money owed based on that credit, the negotiated sales terms, and the resulting sales price. The Department credited MGI with its operating margin on the sale of the grain before paying the grain depositors.

Under Department of Agriculture oversight, MGI successfully sold 975,000 bushels of grain, collecting into the

escrow accounts sufficient funds to pay its grain depositors. After paying the depositors, the Department on June 24, 1991 released over $135,000 (and over $324,000 worth of grain) to MGI, which had filed for Chapter 11 bankruptcy on May 9, 1991.

The bankruptcy trustee for MGI ("trustee") filed this action in federal bankruptcy court to avoid and bring back into the bankruptcy estate, under § 547(b) of the federal Bankruptcy Code, 11 U.S.C. § 547, those funds transferred from MGI to the depositors within the ninety days preceding MGI's May 9, 1991 bankruptcy "petition date." [1] The grain depositors maintained that due to the valid statutory agricultural commodity lien, MGI had no "interest" in the grain and that, in any event, the funds transferred to them for their grain deposits were no more than they would have received had the distribution been made through bankruptcy, either point preventing avoidance under § 547(b). The trustee argued that the Ohio statutory lien was avoidable both under § 545(1) of the Bankruptcy Code because it became effective only when MGI became insolvent, and under § 545(2) because it was not perfected against a bona fide purchaser on the date MGI filed for bankruptcy.

The bankruptcy court entered summary judgment for the farmers, concluding that under Ohio Revised Code § 926.021 the farmers had a valid lien on the grain which arose upon delivery of the grain by the farmers to MGI. The court determined that the lien created by Ohio Rev. Code § 926.021 was a statutory lien pursuant to the

---

[1] The trustee also separately sued the Ohio Agricultural Commodity Fund and Ohio Commodity Advisory Commission. We upheld application of the U.S. Bankruptcy Code against the state. *In re Merchants Grain, Inc. v. Mahern*, 59 F.3d 630 (7th Cir. 1995). However, the Supreme Court granted certiorari, 116 S.Ct. 1411 (1996), and remanded the case to this court to determine whether our decision is still valid following *Seminole Tribe of Florida v. Florida*, 116 S.Ct. 1114 (1996). That case was stayed June 27, 1996, pending the outcome of this appeal.

Bankruptcy Code and could be avoided by the trustee only through application of § 545 subsections (1) or (2).

The bankruptcy court concluded that neither subsection permitted the trustee to avoid the agricultural commodity liens arising under § 926.021. First, the liens could not be avoided under § 545(2) because the property to which they had attached was not in MGI's possession on the date it filed for bankruptcy. Because § 545(2) gives the trustee the powers of a bona fide purchaser "at the time of the commencement of the case," and because there was no longer any property over which the bona fide purchaser might assert his rights, the bankruptcy court concluded § 545(2) was inapplicable.

The bankruptcy court next determined that the trustee could not avoid the liens pursuant to § 545(1). Because Ohio Rev. Code § 926.021 states that the lien "shall arise at the time of the delivery of the agricultural commodity for sale . . .," the lien first became effective upon delivery of the grain to MGI. The bankruptcy court rejected the trustee's argument that by the terms of the Ohio statute the lien first became effective upon insolvency of the debtor, which the trustee argued would permit the trustee to avoid the lien pursuant to § 545(1). The bankruptcy court concluded that because the lien could not be avoided pursuant to either subsection of § 545, the funds transferred to the farmers were payments on a secured debt and were not subject to avoidance under § 547(b).

The trustee appealed the decision to the district court which affirmed on essentially the same grounds the bankruptcy court had used to reach the initial decision. The district court concluded that the Ohio statute created a lien on grain deposits which removed the grain and its proceeds from being considered property of the debtor. As such, its transfer would not constitute an avoidable transfer under § 547(b), which permits avoidance of transfers of "an interest of the debtor in property." The

court rejected the trustee's argument that the lien could be avoided under § 545(1) as a lien that first became effective upon the insolvency of the debtor. Analyzing the Ohio code, the district court reached the same conclusion as had the bankruptcy court below: the lien created by Ohio Rev. Code § 926.021 became effective at the time of the delivery of the grain to the grain handler. The district court also concluded, as had the bankruptcy court, that because § 545(2) evaluates a statutory lien against a hypothetical bona fide purchaser at the time the debtor filed for bankruptcy, and because the grain had been sold, the farmers paid, and the liens extinguished by that date, § 545(2) could not be used to avoid the lien. Finally, the court noted that even had the lien still existed at the time of bankruptcy, it would have been enforceable against a bona fide purchaser pursuant to Ohio law. The trustee appeals.

II.

We review *de novo* both the bankruptcy court's and the district court's conclusions of law. *In re Forum Group, Inc. v. Harrell*, 82 F.3d 159, 162-63 (7th Cir. 1996). We accept the bankruptcy court's conclusions of fact unless they are clearly erroneous. *Id.*

Bankruptcy Code Section 547

The trustee seeks to "avoid" that is, to get back—the money transferred to the farmers before MGI filed for bankruptcy on May 9, 1991. The mechanism for doing so is found in 11 U.S.C. § 547, Bankruptcy Code ("Code"), § 547. Section 547 permits the trustee to avoid certain transfers made before the filing of bankruptcy:

> (b) Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property—(1) to or for the benefit of a creditor; (2) for or on account of an antece-

> dent debt owed by the debtor before such transfer was made; (3) made while the debtor was insolvent; (4) made—(A) on or within 90 days before the date of the filing of a petition; . . . (5) that enables such creditor to receive more than such creditor would receive if—(A) the case were a case under chapter 7 of this title [11 U.S.C. §§ 701 et seq.]; (B) the transfer had not been made; and (C) such creditor received payment of such debt to the extent provided by the provisions of this title [11 U.S.C. § 1 et seq.].

11 U.S.C. § 547.

All five elements must be present for the trustee to avoid a transfer under § 547(b). *Barash v. Public Finance Corp.*, 658 F.2d 504, 507 (7th Cir. 1981). Two elements are of concern to this case: (1) whether the transfers were interests in the debtor's property, as required by the preamble to § 547(b), and (2) whether the transfers permitted the creditors, in this case the farmers, to receive more than they would have through the bankruptcy proceeding if the transfers had not been made as required by the fifth element.

The trustee asserts that the payments made by MGI and the Director to the grain depositors were transfers of MGI's interest in property and that, as general creditors, the farmers would not have received the transfers had they stood in line for payment along with all the other unsecured creditors.

The grain depositors argue that neither element is met. First, the Ohio statutory lien [2] on the grain prevented the transfers from constituting transfers of an "interest of the debtor [here MGI] in property." Second, the same lien placed the grain depositors in the position of secured lienholder creditors who, collecting ahead of unsecured

---

[2] A statutory lien is a lien "arising solely by force of a statute on specified circumstances or conditions." 11 U.S.C. § 101 (53).

general creditors, would have received the transfers through bankruptcy distribution in any event.

The Code does not define "an interest of the debtor in property." "Generally, property belongs to the debtor for purposes of § 547 if its transfer will deprive the bankruptcy estate of something which could otherwise be used to satisfy the claims of creditors." *In re Bullion Reserve of North America,* 836 F.2d 1214, 1217 (9th Cir.), *cert. denied,* 486 U.S. 1056 (1988). In *Begier v. I.R.S.,* 496 U.S. 53 (1990), the Supreme Court concluded that the term "property of the debtor" was coextensive with "interests of the debtor in property" as used in 11 U.S.C. § 541(a)(1). *Id.* at 59 n.3. Section 541(d) clarifies § 541(a) by providing that "property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, . . . becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold." Thus, the interest of the debtor in property "is best understood as that property that would have been part of the estate had it not been transferred before the commencement of bankruptcy proceedings." *Id.* at 58.

A lien is a property right, *Armstrong v. United States* 364 U.S. 40, 46 (1960); *In re Penrod,* 50 F.3d 459, 462 (7th Cir. 1995), and the Code looks to state law to determine the extent of that interest. *In re Freedom Group,* 50 F.3d 408, 410 (7th Cir. 1995) (citing *Barnhill v. Johnson,* 503 U.S. 393, 397-98 (1992); *McKenzie v. Irving Trust Co.,* 323 U.S. 365, 370 (1945)). If the Ohio statutory lien on grain deposits was valid under Ohio law, and not avoidable under the Code, it would deprive MGI, the debtor, from holding equitable interest in the grain to which it held paper title. The lien would prevent the grain in question, or the proceeds from that grain, from

being considered an interest of the debtor in property subject to avoidance under § 547(b). Likewise, if the Ohio statutory liens were valid under Ohio law and not avoidable by the Code, they would create secured creditor status for the grain depositors which would entitle them to be paid before general creditors under bankruptcy laws governing distribution of the bankruptcy estate. *Barash, supra*, at 509; *see, also, In re Hagen*, 922 F.2d 742, 746 (11th Cir. 1991) ("A transfer to a secured creditor in the amount of its lien does not constitute an avoidable preference."; *Deel Rent-A-Car, Inc. v. Levine*, 721 F.2d 750, 756 (11th Cir. 1983) ("The fact that one creditor is paid in full from a source to which other creditors have no right . . . does not entitle . . . the trustee to recover the amount so secured." (quoting *Walker v. Wilkinson*, 296 F. 850, 852 (5th Cir. 1924)). The trustee's ability to employ § 547(b) to avoid the transfers rises or falls on whether the lien created by Ohio statute was both valid under state law and not prohibited under the Code.

The Ohio Statute

Ohio's statutory lien on grain deposits is found in Chapter 926, the portion of its agricultural code dealing with "Agricultural Commodity Handlers." Specifically, the language creating the lien is found in a portion of the agriculture commodity handlers' code immediately following the statute that sets out the powers of the Director of Agriculture:

> § 926.02 **Powers of director of agriculture.**
>
> The director of agriculture shall administer this chapter . . . .
>
> [§ 926.02.1] § 926.021 **Liens on agricultural commodity assets of failed handler; priority.**
>
> (A) [definitions]
>
> (B) A lien shall exist on all agricultural commodity assets of a failed agricutural commodity handler in favor of any of the following:

(1) Claimants including lenders, who possess receipts covering grain owned or stored by the handler;

(2) Claimants who possess written evidence of ownership other than a receipt disclosing a storage obligation of the handler, including tickets;

(3) Claimants who surrendered receipts as part of an agricultural commodity sales transaction but were not fully paid for the agricultural commodity and the handler failed within twenty days after the surrender;

(4) Claimants who possess any other written evidence of the sale of agricultural commodities to the failed handler for which they were not fully paid.

(C) The lien which shall secure all claims described in division (D) of this section, shall arise at the time of the delivery of the agriculture commodity for sale, . . . and shall terminate when the liability of the agricultural commodity handler to the claimant is discharged, provided that the priority of each lien among the respective claimants shall not relate to the date the claim arises but shall be governed by the priorities established in division (D) of this section. The lien claims of all claimants shall be considered to be assigned by operation of this section to the department of agriculture, and in the event of a failure and subsequent liquidation, the lien shall transfer over to assets or proceeds of assets either received or liquidated by the department of agriculture.

(D) In the event of a failure, the director of agriculture shall enforce the lien claims and allocate the proceeds as follows:

(1) First priority against all agricultural commodity assets shall be the following:

(a) Claimants, including lenders, who posses receipts covering grain owned or stored by the agricultural commodity handler.

(b) Claimants who posses written evidence of ownership other than receipts disclosing a storage obligation of the handler

. . . .

This statute explicity creates a lien on grain deposits. But the critical issue in this case is the point at which the liens attached to the grain. To determine when the liens attached, we consider the text of the statute. *Consumer Product Safety Comm'n v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980) ("[T]he starting point for interpreting a statute is the language of the statute itself.") We examine the statute according to the convenional rules of statutory construction; absent statutory definitions, we accord words and phrases their ordinary and natural meaning and avoid rendering them meaningless, redundant, or superfluous; we view words not in isolation but in the context of the terms that surround them; we likewise construe statutes in the context of the entire statutory scheme and avoid rendering statutory provisions ambiguous, extraneous, or redundant; we favor the more reasonable result; and we avoid construing statutes contrary to the clear intent of the statutory scheme. *See e.g., Trustees of Chicago Truck Drivers, Helpers and Warehouse Workers Union (Independent) Pension Fund v. Leaseway Transp. Corp.*, 76 F.3d 824, 828 (7th Cir. 1996); *Welsh v. Boy Scouts of America*, 993 F.2d 1267, 1269, 1272-73 (7th Cir.), *cert. denied*, 114 S.Ct. 602 (1993); *United States v. Hayward*, 6 F.3d 1241, 1245-46 (7th Cir. 1993), *cert. denied*, 114 S.Ct. 1369 (1994); *United States v. Franz*, 886 F.2d 973, 977-78 (7th Cir. 1989).

The trustee argues the phrase in division (B)—"a lien shall exist on all agricultural commodity assets of a failed agricultural commodity handler"—instructs that the lien becomes effective upon "failure," which includes insolvency. We disagree. On the simplest level, "shall exist" does not mean "shall become effective." "Exist" implies "to continue in being." Oxford English Dictionary (2d

Ed. 1989). And "continue in being" implies preexistence. Thus, a plausible plain meaning of division (B) is that a preexisting lien shall continue on agricultural commodity assets of a failed agricultural commodity handler.

This reading of division (B) is confirmed by division (C) which states that "the lien . . . shall arise at the time of the delivery of the agriculture commodity for sale." "Arise" commonly means "originate," "result from," and "come into existence." *Id.* This confirms that the lien comes into existence upon delivery of grain to the agriculture commodity handler and preexists any insolvency of the agricultural commondity handler (unless of course it is delivered after the filing of bankruptcy, which was not the case here).

This reading is consistent with the statutory scheme as a whole. The statute charges the Director of Agriculture with the enforcement of certain liens on agriculture commodities. Division (B) instructs the Director to enforce liens that already exist in favor of certain types of grain depositors, including those who have receipts or other evidence of deposits for sales, storage, or some other transaction. Division (C) sets out how and when the liens are created ("shall arise at the time of the delivery") and how and when they are extinguished ("shall terminate when the liability of the agricultural commodity handler to the claimant is discharged"). Finally, division (D) instructs the Director how to allocate claims among the grain depositor claimants, based on the strength of the receipt they hold (claimants with receipts first, claimants with written evidence other than receipts next, etc.).

The trustee disagrees, arguing that division (B) creates the lien and division (C) merely creates a relation-back date for consideration of statutory liens vis-a-vis other liens, while division (D) allocates priority among holders of agriculture commodity liens arising under this statute. We do not disagree that by creating a statutory lien that arises on deposit, division (C) would assist in setting pri-

orities between one type of secured lien and another. But this effect does not override the clear statutory purpose of division (C). The statute is not concerned with the relationship between statutory grain liens and other liens. The trustee's reading renders division (C) extraneous insofar as the statute instructs the Director to enforce agricultural liens. After all, the Director is not charged with enforcing all liens against a failed agricultural commodity handler, only those liens described in paragraph (B) that are valid pursuant to paragraph (C). By its very terms, the import of division (C) is that the liens the Director is directed to enforce in division (B) (in the priorities dictated by division (D)) are those liens that are in effect—those that arose on delivery and would terminate on discharge.

Ohio's lien-creating statute, read in its entirety and in a manner that does not render any portion meaningless, redundant, or superfluous, creates a lien that arises upon delivery of the grain commodity to the handler. It arises simultaneously with delivery and is only extinguished when liability for the grain has been discharged, that is, when the depositor has been paid. Thus, by statute, the grain handler cannot possess a property interest in grain deposits free from the Ohio agricultural commodity lien unless the lien has been extinguished by payment.

The statute is silent on perfection. The trustee argues that because the lien cannot be perfected it cannot become enforceable. Ohio's other agricultural lien statutes create a similar lien on agricultural products other than grain which requires perfection in order to be valid against a commodity handler. *See, e.g.*, Ohio Rev. Code §§ 1311.55-57 (1991); *In re Peter J. Schmitt Co., Inc.*, 154 B.R. 47, 50-51 (Bankr. D.Del. 1993) (discussing Ohio non-grain (cheese and whipped cream) agricultural liens and perfection requirements). Grain deposits are explicitly excluded from that statue, however, and thus are not subject to its perfection requirement. Ohio Rev.

Code § 1311.55(A)(1) (lien applies to agricultural commodities other than grain commodities covered in chapter 926). The liens were enforceable under Ohio law without formal perfection, as this case illustrates. The Ohio Director of Agriculture enforced the lien claims and allocated the proceeds of the grain sales to the grain depositors pursuant to the statute.

The grain on deposit at the MCI Columbus facility arrived at that facility with a valid lien attached to it pursuant to Ohio statute. The lien was for the value of the grain as dictated by the contract with the handler. Thus, it could only terminate once "the liability of the agricultural commodity handler to the claimant [was] discharged." § 926.021(C). In this case, the depositors were "delayed pricing agreement" depositors whose contracts called for sale and payment on a future date. The contracts were renegotiated by the Director pursuant to the Department's administration of the liens, and the grain was sold in conformity with the new contracts. It appears that, as a result, the grain was sold sooner than it would have been otherwise. In any event, the record indicates that before paying the grain depositors for their grain, the Director credited to MGI its operating margin on the sales. The Director transferred to MGI (or its bankruptcy estate) over $459,000 in cash and grain remaining after enforcement of the liens, however the record does not indicate the extent to which that either failed to meet or exceeded the margin that would have been due to MGI had it still been licensed to operate.

Insofar as Ohio law creates and maintains a lien on the grain deposits, it creates a property interest in the grain, *see In re Penrod*, 50 F.3d at 462 (lien is property interest), *In re Freedom Group*, 50 F.3d 410 (state law defines property interests), that does not pass to the handler until the handler pays the depositor. § 926.021(C). In Ohio, the Director enforces that property interest on behalf of the grain depositor who holds the interest pursuant to the statute. § 926.02 ("The director

of agriculture shall administer this chapter. . . ."); § 926.021(D) ("In the event of a failure, the director shall enforce the lien claims. . . ."). Thus the handler receives title to the grain but no legal, equitable, or property interest beyond the title until the lien is extinguished. The liens unquestionably had not been extinguished at the time the Director enforced them on behalf of the farmers. There is also no dispute that the Director had authority pursuant to state law to enforce the liens. There is, in fact, no dispute that the liens existed.[3]

The Ohio statutory lien on the grain deposits therefore prevents the trustee from meeting the necessary elements of § 547(b). The grain deposits that were sold by the Director within the 90-day period preceding MGI's filing for bankruptcy were never "an interest of the debtor in property." MGI never held an interest in the property that was not subject to the lien which arose upon delivery. However, the trustee argues he seeks to avoid the transfers, not by application of 547(b) directly, but by applying § 547(b)'s 90-day rule to § 545's power to avoid the fixing of a statutory lien.

Section 545

Section 545 states:

> The trustee may avoid the fixing of a statutory lien on property of the debtor to the extent that such lien—
>
> (1) first becomes effective against the debtor—
>
> . . . . .
>
> (D) when the debtor becomes insolvent

[3] Counsel for the trustee acknowledged as much before the bankruptcy court on October 5, 1994. "It is a lien. I don't think there's much dispute about that. But for the reasons that Mr. Ceryak will go into, it is avoidable under 545(1) and under 545(2)." The trustee pursues the same argument on appeal.

> (E) when the debtor's financial condition fails to meet a specified standard;
>
> . . . . .
>
> (2) is not perfected or enforceable at the commencement of the case against a bona fide purchaser that purchases such property at the time of commencement of the case, whether or not such a purchaser exists; . . . .

11 U.S.C. § 545.

The trustee argues application of § 545, either (1) or (2), permits the avoidance of the Ohio liens. The trustee, the farmers, both courts below, and many other court decisions we have reviewed assume the relevance of this statute to avoiding liens.[4] We cannot agree.

Section 545 permits the trustee to avoid, not "a statutory lien," but "the *fixing* of a statutory lien." The Code does not define the phrase "fixing of a statutory lien," and we have found no cases defining the phrase in relation to § 545. However, the Supreme Court has considered the same phrase in detail in its consideration of Code § 522(f) in *Farrey v. Sanderfoot*, 500 U.S. 291 (1991). Like § 545, § 522(f) addresses the avoidance of the "*fixing* of liens," not the avoidance of liens. The Supreme Court carefully analyzed the statutory language common to both § 522(f) and § 545:

> No one asserts that the two verbs underlying the provision possess anything other than their standard legal meaning: "avoid" meaning "annul" or "undo,"

---

[4] *See, e.g., In re Walter*, 45 F.3d 1023, 1027 (6th Cir. 1995) ("Section 545 of the Bankruptcy Code dictates when a trustee can avoid statutory liens."); *In re Loretto Winery Ltd.*, 898 F.2d 715, 717-18 (9th Cir. 1990) ("Section 545 of the Bankruptcy Code, 11 U.S.C. § 545, dictates when a trustee can avoid a statutory lien."); *In re Woods Farmers Cooperative Elevator Company*, 946 F.2d 1411, 1413 (8th Cir. 1991) ("[Section 545 of the] Bankruptcy Code allows the bankruptcy trustee to avoid certain statutory liens."); *In re LMS Holding Co.*, 50 F.3d 1526, 1527 (10th Cir. 1995) (analyzing § 545(2) as a lien avoidance provision).

> see Black's Law Dictionary 136 (6th ed. 1990); H.R. Rep. No. 95-595, pp. 126-127 (1977), U.S.Code Cong. & Admin.News 1978 p. 5787, and "fix" meaning to "fasten a liability upon," Black's Law Dictionary, *supra*, at 637. The statute does not say that the debtor may undo a lien on an interest in property. Rather, the statute expressly states that the debtor may avoid "the fixing" of a lien on the debtor's interest in property. The gerund "fixing" refers to a temporal event. That event—the fastening of a liability—presupposes an object onto which the liability can fasten. The statute defines this pre-existing object as "an interest of the debtor in property." Therefore, unless the debtor had the property interest to which the lien attached at some point *before* the lien attached to that interest, he or she cannot avoid the fixing of the lien under the terms of § 522(f)(1).

500 U.S. at 296 (emphasis in original).

This reading of the statutory language applies to § 545 as well as it does to § 522(f)(1). "There is a natural presumption that identical words used in different parts of the same act are intended to have the same meaning." *Atlantic Cleaners & Dyers, Inc. v. United States*, 286 U.S. 427, 433 (1932). *See also, Gustafson v. Alloyd Co., Inc.*, 115 S.Ct. 1061, 1067 (1995) (same). Moreover, the decision itself cited § 545 for the proposition that other provisions of the Code indicate Congress intended "fixing" to mean a temporal event. *Farrey*, 500 U.S. at 296 n.3.

As the Supreme Court discussed in *Farrey*, Congress' revision of the Code to permit a debtor to avoid the fixing of some statutory liens under 11 U.S.C. § 545 was an exception to the general principle that valid liens obtained before bankruptcy survive bankruptcy and could be enforced on property exempt from bankruptcy distribution. *Id.* at 297.

Because the lien for the full amount of grain deposited arose contemporaneously with delivery, the lien attached

(was "fixed") before MGI held any interest in the grain. MGI acquired the grain subject to the statutory lien. Therefore, MGI held nothing the trustee could prevent a lien from "fixing" upon under § 545(1) or (2). "[U]nless the debtor had the property interest to which the lien attached . . . before the lien attached to that interest, he or she cannot avoid the fixing of the lien . . . ." *Id.* at 296. Thus the lien was not avoidable under § 545.

We recognize, as did the Supreme Court in *Farrey*, that the analysis pursuant to § 545 parallels that used to determine whether the debtor has an interest in the property to begin with. It is the same analysis discussed above in our determination that the Ohio statutory lien prevented MGI from possessing an interest in the grain under § 547(b). It is a temporal analysis. If the lien had been fixed on property of the debtor, that is on the property of MGI, then depending upon when it became effective it may have been avoidable by the trustee. While the fixing of a lien is a transfer in itself, the fixing of a lien may not be avoided by the 547(b) 90-day provision. Section 547(c)(6) states: "The trustee may not avoid under this section a transfer . . . (6) that is the fixing of a statutory lien that is not avoidable under section 545 of this title. . . ." This section thus limits the trustee's authority to employ the § 547(b) 90-day provision to avoid the "fixing of a statutory lien." By the terms of § 547(c)(6), that limit is sequential to the authority of the trustee under § 545 to avoid the fixing of the lien. Thus, in considering statutory liens under § 545, we must do so without benefit of the 90-day avoidance provided by § 547(b).

All of which means the trustee must challenge a statutory lien first by application of § 545 which permits the trustee to avoid the fixing of certain types of liens. If the fixing of the lien is not avoidable under that section alone, the trustee may not apply the § 547(b) 90-day rule to avoid the fixing of the lien. However, if the fixing of the lien is avoidable under § 545, the trustee may apply

the 90-day provisions to recoup any transfers made pursuant to the avoidable lien. *Cf.* Collier on Bankruptcy 547.14 n.4 (§ 547(b) does not prohibit trustee from avoiding transfers in satisfaction of a lien, only the fixing of a lien).

We have also considered the trustee's argument that the Ohio lien prefers Ohio farmers at the expense of out-of-state farmers and creditors and found it without merit. The Ohio statute is nondiscriminatory on its face. It protects depositors of grain in Ohio grain elevators equally, no matter from what state they come. That MGI Columbus was located almost in dead center of the state creates the factual anomaly that only Ohio farmers had grain on deposit. We would expect an elevator facility located near any of Ohio's borders with surrounding farm states to contain grain deposits from out-of-state farmers who would enjoy the same statutory protection as all other grain depositors utilizing the facility. To the extent the agricultural lien statute creates a secured interest in grain deposits in Ohio grain facilities, that interest disadvantages all unsecured creditors equally, both in and outside Ohio. The Code is not inherently hostile to state statutes creating agricultural or other producer liens. "Statutory liens in favor of such beneficiaries as contractors, mechanics, and materialmen secure persons who have contributed to an enhancement of the value of the debtor's estate, and to withhold protection of such liens in bankruptcy cases would give a windfall to the other creditors." 4 Collier on Bankruptcy ¶ 545.01, at 545-6, as quoted in *In re Loretto Winery Ltd.*, 898 F.2d 715, 721 (9th Cir. 1990) (commenting on California's agricultural lien on grapes). The statute's benefits to Ohio farmers at the expense of out-of-state creditors is only incidental and does not create any unconstitutional preference to one state's citizens at the expense of another's. *See Oregon Waste Systems Inc. v. Department of Environmental Quality of State of Or.*, 511 U.S. 93, 114 S.Ct.

1345, 1350 (1994) (nondiscriminatory regulation valid unless burden on interstate commerce clearly excessive in relation to local benefits).

III.

To summarize, the lien at issue in this case fixed upon the grain upon delivery when it was deposited. This prevented MGI from holding a property interest in the grain that would permit the trustee to avoid pursuant to § 547(b) the transfer of the grain proceeds to the farmers within the 90-day period preceding bankruptcy. Because the transfers were payments on a secured debt they could not be avoided under § 547(b). The trustee may not avoid the lien pursuant to § 545 because that section prevents not the avoidance of liens but the avoidance of the fixing of liens on property that is already the debtors'. The farmers in this case were paid out of the proceeds of the sale of the grain on which the lien had fixed upon deposit. The grain was never the property of MGI prior to the fixing of the lien and the trustee may thus not avoid the fixing of the lien or the transfers in satisfaction of the lien.

Accordingly, the district court opinion in AFFIRMED.

A true Copy:

Teste:

Clerk of the United States Court of
Appeals for the Seventh Circuit

APPENDIX B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

Cause No. IP 95-0030-C-M/S

MERCHANTS GRAIN, INC., BY AND THROUGH RECEIVER, EDMUND M. MAHERN,

Appellant,

v.

MARK ADKINS, *et al,*

Appellees.

91-5047-RMV-7A
Bankruptcy Case No.

IN RE: MERCHANTS GRAIN, INC., BY AND THROUGH RECEIVER, EDMUND M. MAHERN,

93-0114
Adversary Proceeding No.

MERCHANTS GRAIN, INC., BY AND THROUGH RECEIVER, EDMUND M. MAHERN,

Plaintiff,

v.

MARK ADKINS, *et al.,*

Defendants.

ORDER

Plaintiff Edmund M. Mahern ("Trustee"), Trustee of Merchants Grain, Inc. ("MGI"), appeals from a decision of the Bankruptcy Court in which that Court found against him in his effort to set aside allegedly preferential transfers. Defendants below are customers of MGI of

Columbus, Ohio, who entered into delayed price agreements with MGI and who received payments from MGI less than ninety days prior to the filing of MGI's bankruptcy. The Ohio Agricultural Commodity Fund and the Ohio Commodity Advisory Commission have intervened in this matter and are appellees, as well as are the individual customers. The Trustee for MGI filed an adversarial complaint in the Bankruptcy Court for the avoidance of preferential transfers pursuant to § 547 of the Bankruptcy Code. This appeal stems from the summary judgment ruling by the Bankruptcy Court adverse to the Trustee.

I. STANDARDS

In reviewing a decision of the bankruptcy court, the district court acts as an appellate tribunal and is governed by traditional standards of appellate review. Specifically, the Court "is constrained to accept the bankruptcy court's findings of facts unless they are clearly erroneous." *In re Excalibur Auto Corp.*, 859 F.2d 454, 457, n. 3 (7th Cir. 1988); *In re Longardner & Associates, Inc.*, 855 F.2d 455, 459 (7th Cir. 1988). "A finding is clearly eroneous if upon review of the entire record the reviewing court is left with the definite and firm conviction that a mistake has been committed." *Graham v. Lennington*, 74 B.R. 693, 695 (S.D. Ind. 1987). "Generally, as long as the bankruptcy judge's inferences are reasonable and supported by the evidence, they will not be disturbed." *Id.*

Conclusions of law made by the bankruptcy court, however, must be reviewed *de novo*. *Excalibur Auto Corp.*, 859 F.2d at 457, n. 3; *Longardner & Associates, Inc.*, 855 F.2d at 459; *In re Bonnett*, No. 87-2102 slip op. at 3 (7th Cir. Dec. 20, 1989). And, where the challenged finding is a mixture of law and fact, the clearly erroneous standard is also inapplicable. *Graham*, 74 B.R. at 965. With these general standards at hand, the issues raised can be addressed.

II. DISCUSSION

The Bankruptcy Court has found, and no one disputes, that MGI owned and operated grain storage facilities in six different states. The Ohio facility located in Columbus, Ohio, is the focus of this action. Resolving this matter involves examining the Ohio statutes that provide the means for dealing with failing or failed grain dealers. That comprehensive statutory scheme was undoubtedly designed to protect Ohio farmers from the consequences of dealing with a poorly managed grain elevator. An important issue in this case is whether Ohio's attempt to solve this problem is in reality an effort to distribute the assets of an insolvent grain dealer to farmer creditors, which effort would be superseded by federal bankruptcy law. *Emil v. Hanley*, 318 U.S. 515 (1943); *Taylor v. Sternberg*, 293 U.S. 490 (1935).

A crucial section of that Ohio law is § 926.021(B) which states as follows:

> A lien shall exist on all agricultural commodity assets of a failed agricultural commodity handler in favor of any of the following: (1) Claimants, including lenders, who possess receipts covering grain owned or stored by the handler; (2) Claimants who possess written evidence of ownership other than a receipt disclosing a storage obligation of the handler, including tickets; (3) Claimants who surrendered receipts as part of an agricultural commodity sales transaction but were not fully paid for the agricultural commodity and the handler failed within twenty days after the surrender; (4) Claimants who possess any other written evidence of the sale of agricultural commodities to the failed handler for which they were not fully paid.

The statute goes on to say in § 926.021(C) that:

> The lien which shall secure all claims described in division (D) of this section, shall arise at the time

> of the delivery of the agricultural commodity for sale, commencement of the storage obligation, or when funds are advanced by the lender, and shall terminate when the liability of the agricultural commodity handler to the claimant is discharged. . . .

The appellees in this matter, the individual farmers (the "Farmers"), are all holders of delayed price contracts. The delayed price contract itself says:

> The fixing of the price of grain is deferred, and may be established by seller at any time, but not later than ————————, and upon demand by seller, the buyer is obligated to pay his regular bid price upon the date of demand for the commodities being priced by the seller. If no such notice is given by seller by the date established in the preceding sentence, the buyer's offered price on that date shall control and the buyer shall promptly give seller written notice of that price, unless a renewal has been written prior to the above expiration date covering the same grain covered by this contract and agreed upon by both buyer and seller.

The agreements also contain the crucial language that in various and sundry wordings, depending on the contract, the Farmer

> fully understand(s) that upon delivery I am transferring title to the Merchants Grain & Transportation and become a creditor of the Merchants Grain & Transportation for the market value of commodities so delivered until the price is established and settlement is completed. If the Merchants Grain & Transportation defaults in its obligation for settlement, I am a common creditor of the Merchants Grain & Transportation for the value of commodities not settled for.

Thus the Farmers, by contract, agreed that by contracting for a delayed price with MGI they would be considered

as common creditors. They also agreed that Merchants Grain & Transportation would own the grain at the time of its delivery to MGI.

The Ohio statute, however, extends the sellers' rights beyond those conferred upon them by the delayed price contract. The statutory scheme gives the Farmer a lien, arising on the date of delivery of the grain, on all the agricultural commodity assets of a failed agricultural commodity handler. Agricultural commodities are defined to include all grains that are deposited with the handler. Ohio Revised Code ("O.R.C.") § 926.02. An agricultural commodity handler is defined in § 926.01(c) as: "any person who is engaged in the business of agricultural commodity handling." Applying simple principles of statutory interpretation indicates that the statute grants to the Farmers, upon their delivery of grain to MGI, and in spite of the acknowledgement in the contract of the Farmers' status as common creditors, a statutory lien on the grain that they deposited as of the date of the deposit.

As long as the elevator is solvent, matters will go smoothly. If, however, statutory financial requirements are not met, the Director of Agriculture (the "Director") may refuse to grant, or may conditionally suspend, a handler's license. These financial requirements are stricter than the federal notion of bankruptcy. That is, grain dealers will be in trouble with the state regulators long before their debts exceed their assets. *See* O.R.C. § 926.06(B); § 926.10.

In this case, the MGI facility in Ohio fell below the statutory financial standard. As the court below found, under O.R.C. § 926.06(B) MGI was required to have a positive current net worth and a total net worth of at least $300,000.00 to be in compliance. The Ohio Department of Agriculture (the "Department") determined, after review of MGI's financial records, the existence of a current net worth deficiency of over $6,000,000.00. After some correspondence between the Department and

MGI, the Director conditionally suspended MGI's Ohio agricultural commodity handler's license on November 8, 1990. For the next two months, the Department allowed MGI to continue to operate, but increased its oversight of the troubled commodity handler. After the Department learned that MGI had written an insufficient-funds check to the federal government, it began a full examination of the debtor's grain records and inventories.

As of January 7, 1991, the Director advised MGI that its license was immediately suspended. Following that unconditional suspension, the Department and MGI began negotiations toward a settlement agreement, which would allow MGI to make good on its agreements with the depositing Farmers. Such an agreement was reached in January, 1991, which benefitted the appellees in this case, although the agreement was not formally executed until May 8, 1991. Under the terms of that agreement, MGI was able to continue in business, selling some 975,000 bushels of grain. The funds realized from those sales were deposited in one of three joint escrow accounts held by Star Bank, an Ohio banking institution, where they earned interest. In order for a check to issue from one of the three joint escrow accounts, it had to be signed by both the Department and MGI.

In the process of implementing the settlement agreement, the Department reached an agreement with the delayed price contract depositors concerning negotiated prices that reflected the current market price. In addition, the Department verified the number of bushels attributable to each depositor and the amount of money owing to each. The grain depositors were paid the negotiated price from the proceeds of MGI's sale of grain, which had been deposited in the joint escrow accounts.

MGI filed for bankruptcy on May 9, 1991, which established the "petition date" for purposes of § 547(b)(4) of the Bankruptcy Code. At certain times within ninety days of the petition date, the Farmers received payoffs

of their claims under the deferred payment contracts. The original complaint in this matter was filed by the Trustee in order to avoid those transfers and to bring the amounts of money transferred back into the bankrupt estate. At issue is whether the statutory scheme that enabled the Department to direct the above-described transaction, constitutes an attempt by Ohio to distribute the assets of an insolvent grain dealer in violation of the policies behind federal bankruptcy law. If that is the case, then the transfers of money from the escrow accounts, within ninety days of the petition date, would be considered preferential transfers and would be subject to avoidance by the Trustee.

Section 547(b) of the Bankruptcy Code provides as follows:

> Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property—(1) to or for the benefit of a creditor; (2) for or on account of an antecedent debt owed by the debtor before such transfer was made; (3) made while the debtor was insolvent; (4) made —(A) on or within 90 days before the date of the filing of a petition; or (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and (5) that enables such creditor to receive more than such creditor would receive if—(A) the case were a case under Chapter 7 of this Title [11 U.S.C. §§ 701 *et seq.*]; (B) the transfer had not been made; and, (C) such creditor received payment of such debt to the extent provided by the provisions of this title [11 U.S.C. § 1 *et seq.*].

The Farmers wish to focus the Court's attention on the first clause of this section, arguing that the transfer of the funds from the state-operated MGI to them was not a transfer "of an interest of the debtor in property." Their position is that despite the delayed pricing contracts' ex-

plicit statement that MGI owns the grain in question, the parties contracted against the backdrop of the Ohio statutory scheme. That scheme specifically enlarged the Farmers' rights to include a lien on the agricultural commodity assets of MGI.

By granting a lien to grain depositors, which arises at the time of delivery of the agricultural commodity for sale or commencement of the storage obligation, the Ohio statute removes the grain and its proceeds from consideration as property of the debtor. This is so because "property of the debtor" has been defined as that property that would be available to the debtor for distribution to creditors in a bankruptcy proceeding. *Begier v. Internal Revenue Service,* 110 S. Ct. 2258, 2262-63 (1990); *In re Bullion Reserve of North America,* 836 F.2d 1214, 1217 (9th Cir. 1988).

By definition, a lien is an encumbrance on property for the payment of some obligation, or performance of a duty. Black's Law Dictionary, Sixth Ed. Consequently, the possessor of the encumbered property enjoys less than full ownership rights in such property. That is because "[l]iens are property rights and the forfeiture of such rights is disfavored." *In re Penrod,* 50 F.3d 459, 462 (7th Cir. 1995); *see* 11 U.S.C. § 101 (37) (a lien is an interest in property). It follows, then, that property to which a lien is attached is not property available to a debtor for distribution to creditors generally in a bankruptcy proceeding. *See Penrod,* 50 F.3d at 463 (at the start of a bankruptcy proceeding, liens of secured creditors are not the debtor's property).

The Trustee, on the other hand, argues that this lien is not valid, because it could be avoided under § 545 (1) of the Bankruptcy Code, thereby making the payments which went to the Farmers, payments on unsecured debts. The Bankruptcy Code section on which the Trustee relies provides that

> The trustee may avoid the fixing of a statutory lien on property of the debtor to the extent that such lien—
>
> (1) first becomes effective against the debtor—
>
> (A) when a case under this title concerning the debtor is commenced;
>
> (B) when an insolvency proceeding other than under this title concerning the debtor is commenced;
>
> (C) when a custodian is appointed or authorized to take or takes possession;
>
> (D) when the debtor becomes insolvent;
>
> (E) when the debtor's financial condition fails to meet a specified standard; or
>
> (F) at the time of an execution against property of the debtor levied at the instance of an entity other than the holder of such statutory lien;

11 U.S.C. § 545(1). The question, of course, is whether the Ohio statutory lien becomes effective against the debtor when an insolvency proceeding concerning the debtor is commenced, or when the debtor becomes insolvent, or when the debtor's financial condition deteriorates to a specified level.

The Trustee argues that the Ohio statute describes the existence of the lien only in the context of a "failed" agricultural commodity handler, and concludes from that reference that the lien becomes effective upon the insolvency or other financial deterioration of the debtor's business. In support of this argument, the Trustee refers to the definition of "failure" in the Ohio statute. Failure is defined as including the inability to financially satisfy claimants, a public declaration of insolvency, the revoca-

tion of the commodity handler's license when it owes money to claimants, or other circumstances relating to maintaining a valid license. O.R.C. § 926.021(A)(2). However, inferring that the legislature meant the lien to arise only when the commodity handler becomes financially distressed would not be reasonable, because it would render a more specific portion of the statute superfluous. Moreover, fundamental principles of statutory construction require that the more specific provision takes precedence over the more general. *See Green v. Bock Laundry Mach. Co.*, 490 U.S. 504, 524 (1989).

The Ohio statutory scheme specifically states that the lien becomes effective at the time of the delivery of the grain to the grain handler. O.R.C. § 926.021 (C). It also goes on to say, "In the event of a failure, the director of agriculture shall enforce the lien claims and allocate the proceeds . . . ." O.R.C. § 926.021 (D). This more specific delineation of the inception of the statutory lien takes precedence over any general reference to a lien coming into existence when the commodity handler has failed.

The statute also specifically denotes when the lien ceases to exist. The statutory lien is extinguished upon the payment of the obligation to the depositor. The Ohio statutory scheme is unlike any other scheme from any other state cited by the Trustee. By statute, the State of Ohio gives a lien to the grain depositor that arises from the time the grain is placed in the elevator and is extinguished at one of two times, either after the grain elevator operator falls below the prescribed financial standard and the claim is paid through the Department of Agriculture, or at the time the elevator operator pays the depositor.

In this Court's view, the Ohio statutory lien is not voidable under § 545 (1) of the Bankruptcy Code, because it becomes effective at the time the grain is deposited

rather than at the time the insolvency is suspected. The Ohio statutory scheme is quite different from the scheme in Illinois cited in *Gorenz v. State of Illinois Dep't of Agriculture*, 653 F.2d 1179 (7th Cir. 1981).

In that case, acting pursuant to Illinois Revised Statute, Chapter 127, § 40.23 (1979), the Illinois Department of Agriculture seized grain in the possession of John Gorenz and subsequently sold the grain and retained the proceeds of the sale. The trustee attempted to avoid those transfers and bring the resultant $38,000.00 back into the bankruptcy estate. Section 40.23 gives the Illinois Department of Agriculture the power:

> To control surety bonds and trust funds and to establish trust accounts and bank accounts in adequately protected financial institutions, to hold monies received by the Director of Agriculture when acting as trustee, to protect the assets of licensees for the benefit of claimants, to collect and disburse the proceeds of such bonds and trust funds when acting as trustee on behalf of claimants without responsibility for the management and operation of discontinued or insolvent businesses, such funds or additions thereto in which the state of Illinois has no right, title or interest.

The bankruptcy court and the district court in *Gorenz* held that the Department was required to surrender the proceeds of the grain sale to the trustee. The appellate court overturned that decision, finding insufficient evidence of the ownership of the grain that was seized. If the bankrupt was found to own the grain, the Department could not resist the jurisdiction of the bankruptcy court, because the action of the State of Illinois would have been an attempt to distribute assets of an insolvent grain dealer to farmer creditors and would thus be superseded by federal bankruptcy proceedings.

In the case before this Court, however, even though the contracts seem to indicate that the owner of the depos-

ited grain is MGI, the State of Ohio impressed a statutory lien upon that property, which removes it from a bankruptcy consideration as "property of the debtor." The point is, the deposited grain was not wholly the property of the debtor under Ohio law. This finding would be true regardless of whether there was a bankruptcy proceeding pending.

The State of Ohio selected this method by which to protect its farmers from financially troubled warehousers. It has done so in a different fashion than did the State of Illinois. Illinois impressed no liens upon the grain, and the liens at issue here are not avoidable by the trustee pursuant to the very language of the Bankruptcy Code. The Bankruptcy Court was therefore correct in its assessment and in its denial of the Trustee's complaint for avoidance of preferential transfers. If the Ohio statute had provided that the lien arose on the event of financial difficulty, this case would be different.

The reasoning of *In re Loretto Winery Limited*, 898 F.2d 719 (9th Cir. 1990), is similar to that used in this matter. Therein a statutory lien was upheld against the trustee's attack, which lien arose on the delivery of product to the processor. The California and the Ohio statutes are based on very similar policies. As in the situation in which a mechanics lien arises, the farmer has applied his labor and resources to produce the product that then increased the value of the debtor's estate. This places the farmer in a different class than general creditors, who have only a pecuniary interest in the estate. To allow general creditors to share equally with the farmers in the estate would unjustly enrich the general creditors at the expense of the farmer's labor. Consequently, the California and Ohio legislatures have successfully endeavored to place the farmers in a different class of creditors than the general creditors, which is a class analogous to secured creditors.

The Trustee also argued that the Ohio statutory lien is avoidable pursuant to § 545 (2), which provides that:

> The trustee may avoid the fixing of the statutory lien on property of the debtor to the extent that such lien—
>
> (2) is no perfected or enforceable at the time of the commencement of the case against a bona fide purchaser that purchases such property at the time of the commencement of the case, whether or not such a purchaser exists

5 U.S.C. § 545 (2) (emphasis added). The statutory lien at issue, however, did not exist at the time of the filing of this bankruptcy, because the claims secured by the lien were already extinguished.

In addition, a statutory lien in Ohio is exempted from the requirement of perfection otherwise required by the Ohio version of the Uniform Commercial Code. Likewise, this lien is not the traditional "secret" lien that is not protected by the law. This Court agrees with the Farmers' argument that this lien has been created by the Ohio General Assembly and is a matter of public record. Because these liens are common in the agricultural industry, those in the industry would be aware of their existence. Any creditors who do business with the debtor would most likely be involved in regular business activity with the grain industry, and consequently they would know of the Ohio statutory lien. And even if they did not, they would be bound by the laws of the states in which they do business, so that a bona fide purchaser in this context would have knowledge, or be chargeable with knowledge of the statute.

For all these reasons, the opinion of the Bankruptcy Court that these transfers may not be avoided as preferential transfers by the Trustee is UPHELD.

IT IS SO ORDERED this 7th day of June, 1995.

/s/ Larry J. McKinney
LARRY J. MCKINNEY, Judge
United States District Court
Southern District of Indiana

APPENDIX C

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

Case No. 91-5047-RWV-7A

IN RE: MERCHANTS GRAIN, INC.,
Debtor

Adversary Proceeding No. 93-0114

MERCHANTS GRAIN, INC. by and
through Receiver Edmund M. Mahern
Plaintiff

vs.

MARK & CHRIS ADKINS, *et al.*,
Defendants

and

OHIO AGRICULTURAL COMMODITY FUND;
and OHIO COMMODITY ADVISORY COMMISSION,
Intervenors

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This matter came before the Court upon the filing of the (i) Defendant's Motion for Summary Judgment filed by the defendant John Timmons on March 23, 1994, (ii) the Motion for Summary Judgment filed on May 9, 1994, by the intervenors, the Ohio Agricultural Commodity Fund and the Ohio Commodity Advisory Commission (the "Intervenors"), (iii) the Summary Judgment Motion

filed by the twenty-two defendants represented by Ricketts & Onda Co., L.P.A. on or about July 15, 1994, (iv) the Plaintiff's Cross-Motion for Partial Summary Judgment filed by Edmund M. Mahern, the Trustee of Merchants Grain, Inc. ("MGI"), on June 3, 1994, and (v) the respective responses and relevant pleadings filed with this Court.

The Court held a hearing on this matter on October 5, 1994, after which time the parties filed additional pleadings with the Court. This matter is now ready for the Court's consideration, and being duly advised, now finds the facts and states its conclusions of law as follows:

Findings of Fact

1. MGI owned and operated grain storage facilities in six (6) states, including one facility in Ohio.

2. Debtor's only Ohio facility was located in Columbus, Ohio.

3. Debtor's Columbus, Ohio facility was a grain terminal servicing many counties, and was not simply a grain elevator. This grain terminal offered larger capacity and additional services compared to an average grain elevator, including large blending capabilities and railroad transportation access.

4. At all relevant times, there was only one other grain facility in central Ohio with comparable capabilities available to the Defendant grain depositors.

5. If Debtor's Columbus, Ohio grain terminal had been completely shut down during harvest time, the grain depositors contemplating using the services of Debtor might have suffered financial losses. Those depositors with future contracts would not have had a ready buyer and would have been forced to sell their grain elsewhere at the regular cash bid which was substantially less than the prices set forth in the future contracts.

6. The Ohio Revised Code, O.R.C. Chapter 926.01 *et. seq.* was applicable to MGI's operations in Ohio.

7. O.R.C. section 926.02 provides that the Director of Agriculture shall administer Chapter 926 of the Ohio Revised Code.

8. Pursaunt to O.R.C. section 926.04, no person shall handle agricultural commodities within the State of Ohio without first obtaining a handlers license issued by the Director of Agriculture.

9. O.R.C. section 926.05 provides that each person desiring to obtain or renew a handlers license shall file an application annually with the Director of Agriculture.

10. O.R.C. section 926.06(B) requires that each handler have a specified net worth based on the volume of grain it handles to meet its obligations rising out of its operation as a handler. This subsection set forth that each applicant for a handlers license or renewal thereof, shall have and maintain current assets equal to or greater than current liabilities and a total net worth of at least ten cents per bushel for the total number of bushels of agricultural commodities that the applicant handled during the immediately preceding twelve month period to cover any indebtedness arising from the applicant's operations as a licensed handler.

11. O.R.C. section 926.10 provides that the Director of Agriculture may refuse to grant or may suspend or conditionally suspend a handler's license, without prior hearing, when he determines that there is reasonable cause to believe that the applicant or licensee does not have the assets specified in Section 926.06, does not have its obligations for agricultural commodities purchased under delayed price agreements secured or represented as required under Division (B) or (C) of O.R.C. 926.29, does not have in its possession sufficient agricultural commodities to cover the outstanding receipts or tickets issued or assumed by it under the bailment agreements, or has failed to maintain accurate and complete records and accounts.

12. O.R.C. section 926.021 provides that claimants acquire a lien on all agricultural commodity assets of a

failed agricultural commodity handler, which lien arises at the time of delivery of the agricultural commodity for sale or storage.

13. O.R.C. section 926.06(B) requires all licensed agricultural commodity handlers to maintain current assets equal to or greater than current liabilities ("current net worth" or "working capital").

14. The Department received a financial statement from Debtor on August 31, 1990, and analyzed it on September 4, 1990.

15. Under O.R.C. section 926.06(B), Debtor was required to have a positive current net worth and a total net worth of at least $300,000.00.

16. The Department's review of Debtor's financial records revealed a current net worth deficiency of $6,061,447.00.

17. Upon learning of the current net worth deficiency, pursuant to O.R.C. section 926.10(G), the Department could have suspended Debtor's agricultural commodity handlers license and closed Debtor's Columbus, Ohio facility. After its investigation, the Department declined to take this action immediately.

18. On September 27, 1990, the Department sent a letter to Debtor saying that the Department's review of Debtor's financial statement indicated that Debtor had a current net worth deficiency of $6,061,447.00.

19. This letter stated that Debtor had three options available to correct the financial deficiency. Debtor could:

(a) Post a surety bond from a corporate surety company;

(b) Obtain an irrevocable letter of credit issued by a bank that is authorized by the State of Ohio or the United States to issue such letters; or

(c) Have an individual execute an indemnity agreement whereby an individual would pledge personal

assets for the benefit of the commodity creditors should Debtor default in its obligations to these creditors.

20. The September 27, 1990 letter demanded a response from Debtor by October 3, 1990. The Department received no response from Debtor with regard to the Department's letter of September 27, 1990. On October 16, 1990, the Department sent a letter to Debtor advising that the Department still had received no response from Debtor. This letter, which provided notice under O.R.C. section 926.14, required Debtor to post an irrevocable letter of credit.

21. Subsequently, the Department received a letter dated October 22, 1990 from BancOhio National Bank, Debtor's primary secured lender, indicating that it was working with Debtor to resolve the financial problems. At about the same time, the Department received a similar letter from Debtor, referring further to BancOhio.

22. The Department again reconsidered suspending MGI's license. However, in doing, so, the Department also had to consider the impact closing the facility would have on the community. By this time, fall harvest was well under way. MGI was vital to the central Ohio agricultural community. It was a terminal facility with railway access, and no other facility of this size and magnitude existed within a reasonable distance of MGI that could accommodate all of MGI's depositors. Closing the facility would pose a severe hardship and would seriously burden farmers and depositors who did business with MGI.

23. Many customers of MGI had future delivery contracts with the elevator facility. The grain prices under these contracts generally were significantly higher than current grain market prices. If the Department closed MGI it would have left many farmers and other customers with no alternative but to cash sale their grain. It is likely that even if these individuals could have found

alternate buyers, as grain prices are generally lower during harvest, the prices would not have been as high as that set by the future delivery contracts, resulting in a loss to the depositors.

24. When Debtor persisted in its failure to comply with the requirements of O.R.C. sections 926.06 and 926.14, the Director of the Ohio Department of Agriculture sent a letter to Debtor on November 8, 1990 advising it that its agricultural commodity handler's license was conditionally suspended (the "Conditional Suspension Letter").

25. A conditional suspension was one option available to the Department under O.R.C. section 926.10. The Department could have fully suspended Debtor's license.

26. The Conditional Suspension Letter further required that all grain obligations were to be covered 100 percent in either grain on hand or cash deposited in a segregated bank account, located in the State of Ohio, for the benefit of the agricultural commodity depositor's special account ("Indemnity Fund"). For purposes of the conditional suspension, "grain obligations" included cash transactions, delayed price deposits, basis contract deposits, deferred payment and bailment grain deposits.

27. After the conditional suspension of Debtor's license in November, 1990, the Department increased its supervision over Debtor's Columbus, Ohio facility, scrutinizing its operation and frequently dispatching employees to the facility to oversee operations and to review records.

28. Debtor still did not correct its capital deficiency as requested by the Department and as required by the O.R.C. Chapter 926.

29. In mid-December, 1990, the Department again began receiving information that Debtor was experiencing financial difficulties. The Department increased its supervision of MGI, but could find no further indication of financial difficulties at its Columbus, Ohio facility. Then, in late December, the Department received a telephone

call from the sate ASCS office (an agency of the federal government), indicating that a check issued to it by MGI had been returned for insufficient funds. The Department immediately began a full examination of Debtor's grain records and inventories. However, before the Department completed its examination, MGI voluntarily closed its Columbus, Ohio facility.

30. Pursuant to a letter dated January 7, 1991, the Director of Agriculture advised Debtor that its license was immediately suspended.

31. Beginning in January, 1991, the Department and Debtor began negotiations toward a Settlement Agreement that would allow Debtor to liquidate the grain it had on hand and the grain receivables at the Columbus, Ohio facility to assure that the grain depositors who had deposited or sold grain at Debtor's Columbus, Ohio facility would be paid. In a letter dated January 9, 1991, the Department set forth the terms of the settlement.

32. The Department and Debtor reached an agreement and carried out the terms of the Agreement in January, 1991, although the Agreement was not formally executed until May 8, 1991 ("Settlement Agreement").

33. Pursuant to a letter dated January 11, 1991, the Department granted a temporary reprieve to the suspension of Debtor's license to allow Debtor to comply with the terms of Settlement Agreement.

34. Under the terms of the Settlement Agreement, the Department and Debtor sold grain located at the Columbus, Ohio, facility and liquidated the grain receivables.

35. This process lasted nearly two months and resulted in the sale of 975,000 bushels of grain.

36. Although it is unclear from the papers currently before the Court whether the terms of all payments were handled in the manner intended, it appears that payments from the sale of this grain and on the grain receivables

were intended to be made jointly to the Department and Debtor.

37. These funds were deposited in one of three joint escrow accounts. Separate escrow accounts were established for delayed price and basis contract obligations, grain payable obligations, and checks issued by Debtor but returned for insufficient funds ("NSF Checks"). The escrow accounts were held by Star Bank where they earned significant interest.

38. All checks drawn on the three joint escrow accounts were signed jointly by the Department and Debtor.

39. Under the terms of the Settlement Agreement, the Department issued a temporary stay of the full suspension of Debtor's license to allow Debtor to sell the grain pursuant to the Settlement Agreement.

40. Although Debtor was authorized to sell the grain, the Department was consulted as to the price, and monitored the facility's day-to-day operations.

41. Under the terms of the Settlement Agreement, the Department contacted all grain depositors and informed them of the procedure established to process and pay their claims.

42. The Department arranged for all depositors to sign agreements which set forth the terms of payment. Delayed price and basis contract depositors agreed to accept the market price on the day of the sale as the contract price. Contract depositors were paid the contract price. Holders of NSF checks were paid the full amount of the check.

43. The Department verified the number of bushels involved with each depositor and the amount of money owing to each depositor. The Department allowed all discounts and set off any accounts receivable. The Depart-

ment also allowed Debtor to collect its operating margin on the sale of grain prior to paying depositors.

44. Under the terms of the Settlement Agreement, if any of the three joint escrow accounts had a surplus, the surplus was to be transferred to one of the other escrow accounts if such account had a deficiency.

45. If any surplus funds remained after the payments from all three accounts were completed, the surplus was to be deposited at National City Bank, formerly known as BancOhio National Bank. National City Bank asserted that it held a perfected lien on grain owned by Debtor, although it was the Department's position that BancOhio's lien was subordinate to the lien granted under O.R.C. section 926.021. The issue of the priority of lien is not before this Court because the Settlement Agreement provided that the proceeds paid into the escrow account were for the benefit of and to be used to satisfy first, the claims of the depositors, and second, to the extent funds remained, the claims of BancOhio.

46. Under the terms of the Settlement Agreement, Debtor had no right to the grain, proceeds thereof, or funds in the escrow accounts. These funds were held jointly in the name of the Department and Debtor.

47. Pursuant to a letter dated February 21, 1991, the Director of Agriculture revoked Debtor's license, except to the extent necessary to effectuate the terms of the Settlement Agreement.

48. Operating under the Settlement Agreement, Debtor liquidated the grain receivables and grain on hand at the Columbus, Ohio facility and deposited the proceeds in the joint escrow accounts. Defendant grain depositors were paid from these joint escrow accounts with checks executed by both Debtor and the Department.

49. After payment in full to the depositors, the Department released its claim to the funds and allowed $135,472.18 to be transferred to BancOhio National Bank.

50. On June 24, 1991, the bankruptcy estate of Debtor obtained the sum of $168,901.19 from the Department representing the funds remaining from the escrow accounts.

51. The Department also turned over to the Debtor grain from Debtor's Columbus, Ohio facility with a total estimated value of $324,183.08.

52. It appears as if the Department did everything in its power to try to work through the situation to protect the depositors without having to suspend MGI's license. The Department tried to balance the interests of the depositors, the farmers and the community. All actions taken were consistent with the statute under which the Department operated. This Court finds no fault on the part of the Department for taking the action it took to protect the depositors. If any, this Court commends the Ohio legislature for having the foresight to enact the legislation which gave the Department the authority to act in this situation.

Conclusions of Law

1. This Court has jurisdiction over the parties and the subject matter of this action pursuant to 28 U.S.C. section 1334(b), Title 11 of the United States Code, and the General Order of Reference issued by the United States District Court for the Southern District of Indiana.

2. Venue of this adversary proceeding is proper in the Court and Division pursuant to 28 U.S.C. section 1409. This Court has authority to hear and determine this adversary proceeding and to grant the relief requested as a core proceeding pursuant to 28 U.S.C. section 157 (b)(2)(H).

3. The funds transferred by Debtor to Defendants were not available for payment to Debtor's general unsecured creditors at the time the funds were transferred.

4. The funds transferred by Debtor to Defendants were earmarked for payment to Defendants pursuant to

the Conditional Suspension Letter dated November 8, 1990, from the Ohio Department of Agriculture to the Debtor and pursuant to the settlement reached in January, 1991. Under the terms of the conditional suspension, Debtor did not control the funds in the escrow accounts to the extent that the funds became property of the estate. *See, Coral Petroleum, Inc. v. Banque Paribas-London*, 797 F. 2d 1351 (5th Cir. 1986); *In re Network 90, Inc.*, 126 B.R. 990 (N.D. Ill. 1991).

6. The transfer of funds by Debtor to Defendants did not result in a diminution of Debtor's bankruptcy estates. See, *In re General Office Furniture Wholesalers, Inc.*, 42 B.R. 232 (Bkrtcy. E.D. Va. 1984).

7. The funds transferred by Debtor to Defendants were held in a constructive trust, with the Debtor and the Ohio Department of Agriculture acting as the constructive trustees, for the benefit of the Defendants. See, *In re Computer Input Services, Inc.*, 33 B.R. 292 (Bkrtcy, E.D. Pa. 1983); *Ferguson v. Owens*, 459 N.E.2d 1293 (1984).

8. The funds transferred by Debtor to Defendants were held in escrow by Debtor and the Ohio Department of Agriculture for the benefit of Defendants. *See, In re Cedar Rapids Meats*, 121 B.R. 562 (Bkrtcy. N.D. Iowa, 1990).

9. The funds transferred by Debtor to Defendants did not constitute property of the Debtor as mandated by Section 547 of the Bankruptcy Code and are not avoidable as preferences. *See, In re Bullion Reserve of North America*, 836 F.2d 1214 (9th Cir. 1988).

10. The transfer of funds from Debtor to Defendants did not enable Defendants to reecive more than they would have received if the case were a case under Chapter 7 of the Bankruptcy Code; the transfer had not been made; and such creditor received payment of such debt to the extent provided by the provisions of the Bankruptcy Code.

11. Defendants had a valid lien pursuant to section 926.021 of the Ohio Revised Code on all agricultural commodities and all agricultural commodity assets, which lien arose at the time of delivery of the grain by Defendants to Debtor.

12. At the hearing on the motions for summary judgment held on October 5, 1994, the Trustee conceded that this lien is a valid lien between the grain storage facility and the grain depositor. The only remaining issue is whether this lien is avoidable by the Trustee as a statutory lien under either section 545(1) or section 545(2) of the Bankruptcy Code.

13. The lien created by O.R.C. section 926.021 is a statutory lien, as defined by section 101(53) of the Bankruptcy Code. Therefore, as a statutory lien, the lien provided by O.R.C. section 926.021 may be avoided by a bankruptcy trustee only under one of the four circumstances described in the subsections of section 545 of the Bankruptcy Code. Subsections 3 and 4 do not apply. Therefore, in order to be avoided by a bankruptcy trustee, the trustee has the burden of proving either that the statutory lien is avoidable under subsection 1 or under subsection 2 of section 545 of the Bankruptcy Code.

14. The lien provided by O.R.C. section 926.021 cannot be avoided under section 545(2) because the property to which the lien attached was not in the Debtor's possession on the date of the filing of the bankruptcy petition. *See, Matter of Lowery Brothers, Inc.*, 589 F.2d 851 (5th Cir. 1979). Section 545(2) gives the trustee the powers of a bona fide purchaser purchasing property "at the time of the commencement of the case". All of the transfers under scrutiny in this proceeding concluded prior to the date of filing of the bankruptcy petition, and therefore, the Trustee has no property against which to assert his rights as a bona fide purchaser.

15. The lien provided by O.R.C. section 926.021 cannot be avoided under section 545(1). Section 926.021(C)

provides that the lien "shall arise at the time of delivery of the agricultural commodity for sale . . ." The lien, therefore, first became effective upon delivery of grain by Defendants to Debtor. The Trustee's argument that this lien first becomes effective when it becomes enforceable by action after default is not supported by the language of the statute. The reference to a "failed agricultural commodity handler" in section 926.021(B) merely sets forth the assets against which the Director may enforce the lien which enforcement power is in conformity with his seizure powers under O.R.C. section 926.14(B). This interpretation is reinforced by section 926.021(D) which authorized the Director of the Department of Agriculture to enforce the lien in the event of a failure. The lien first becomes effective upon delivery of the grain for sale; upon a "failure" the Director may enforce the lien upon behalf of the claimants.

16. The funds transferred by Debtor to Defendants were payments on a secured debt and are not subject to avoidance under section 547(b).

17. The arguments of counsel, pleadings, affidavits, and exhibits submitted in this matter show that there are no genuine issues as to any material facts and that Defendants are entitled to judgment as a matter of law.

18. The Defendants' Motions for Summary Judgment shall be granted and the Plaintiff's Cross-Motion for Summary Judgment denied for the reasons set forth above.

19. The Court will make a separate judgment entry consistent with the findings of fact and conclusions of law set forth herein.

Date Dec. 19, 1994

/s/ Frank J. Otte
FRANK J. OTTE
Bankruptcy Judge

APPENDIX D

List of All Parties to the Proceeding Below

PETITIONER

Edmund Mahern, Trustee for Merchants Grain, Inc.

RESPONDENTS

Mark and Chris Adkins
Dick Brenner
Charles Dresbach & Son
Gary Graham
Jack Jahn
Jim Jahn
Phill Leinaker Farm
Ohigro, Inc.
John Perry
Dean Pontius
Steve Pontius
Robert Reelhorn
Myrtle Sawyer
Larry Starling
Marvin Yutzy
John Bauder
Bethel Road Investments, Inc.
Kenny Brandel
Ken Buell
Jacob Caldwell Heirs
Delbert Crook, Jr.
Cy Cupp
D&C Enterprises
Dawson Farm
Doug Dawson
Dean and Chris DeMatteo
Glen Elfrink
Beverly Evans
Falers Feed Store, Inc.
Fran-Mar Farms
Robert Fuller
Mary Hoffman
Carl Hunsinger
John Jahn
Jefferson Savings Bank
Kennedy Farms
Dr. William Krauss
Lamp Family Farms
John F. Lane
Phill Leinaker
Clarence Mauger
Allen Miller
E. J. Miller
Ralph Miller
Edwin Miller
Wilma Miller
Mitchagri
James Mitchell, Jr.
Robert Carl Mitchell
Richard Montgomery
Doug Mulpas
Ohio Corn Marketing Program
Osborne Farms
P & C Farms
Vance Parkinson
Charity Parkinson
John Perry
Keith J. Quick
Rayner Farm

Judy (Peterman) Reelhorn
River City Farm Supply
John G. Roby
James Rogers
Rick Ross
William Saum
Scioto Valley Farms, Inc.
Ruth Shank
Sharp Brothers
Carolyn Shaw
Gene Smart
Steve Smith
Snell Brothers
Dave Thomas
Thornville Elevator
John Timmons
Mrs. Pryor Timmons
Timmons Heirs
Jack Utzinger
Old Republic Co.
Walnut Creek Farms
Walnut View Farms
Steve Weber
Jay Writsel
Marlin Yutzy
Robert Bieber
Steve Bowling
Jeff Chattin
M. E. Detwiler
Scott Dever
Walter Durett
Jeff Ehman
Raymond Fling
Ted Forman
Rankin Gibson
Edwin Helser
Eugene Hupp
J & K Farms
Kilbarger Farms
Freda Krohn
Tim Leinaker Farm
Robert L. Mitchell
Linda Newell
Jim O'Hara
Piper, Allen & Dwight
Mike Rager
Edna Reiselt
Kenneth Sanders
Greg Schreck
Wilmer Schrock
Howard Siegrist
Walter Starkey
Vernon Tharp
Robert Thomas
William Thomas, Jr.
Mike Tickson
Matilda Totten
John Trapp
Reed Westervelt
Jeff Williams
Greg Yutzy
Clair Zimmerman
Linda Andrews
Larry Augenstein
Robert Belt
Richwood Bank
Farmers Home Administration
Candlehill Farm
Jim Clark
Howard Delamatre
Francis Dunlap
Larry Ellinger
Marvin Eyman
Farmers National Co.
Guy Geiger

J. E. Geiger
Phyllis Graham
Andrew Green
E. Kenneth Hadden
Mark Heister
Herron Farms
Matthew Hoover
William J. Hunzicker
J & J Partnership
David Jackson
Tom Jennings
Larry Kuhlwien
Walter Kull
Linda Lee Farms
Randy Longshore
Mrs. Forrest Lones
Fred L. Lones
Jack McCabe
John McKitrick
McKitrick Properties
Gary Miller
Jerry Miller
Ralph Murphy
Ohigro-South
PFK, Inc.
James E. Paxton
Mary Lou Piper
Radco
Neil Rammelsberg
Rene Schreck
John E. Scott
Roy Speakman
Richard L. Stockberger
Robert and
William Thomas, Jr.
Union County ASCS Office
Warrington Farms
Wayview Farms, Inc.
West Farms
Edgar Willey
Roger Wiseman
Hans Wooster
Earl Yutzy

INTERVENOR RESPONDENTS

Ohio Agricultural Commodity Fund
Ohio Commodity Advisory Commission

Supreme Court, U.S.
FILED
JAN 2 1997
CLERK

No. 96-831

In The
SUPREME COURT OF THE UNITED STATES
October Term, 1996

EDMUND M. MAHERN, TRUSTEE,
FOR MERCHANTS GRAIN, INC.,
Petitioner,

v.

MARK AND CHRIS ADKINS, ET AL.,
Respondents,

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

---

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

BETTY D. MONTGOMERY
Attorney General
JEFFREY S. SUTTON
State Solicitor
Counsel of Record
SIMON B. KARAS
CHERYL D. MINSTERMAN
Assistant Attorneys General
30 East Broad Street
17th Floor
Columbus, Ohio 43215
(614) 466-8980

WILLIAM B. LOGAN, JR.
Luper, Sheriff & Neidenthal
50 West Broad Street
Suite 1200
Columbus, Ohio 43215
(614) 221-7663

Counsel for Intervening Respondents
The Agricultural Commodity Depositors Fund and The Commodity Advisory Commission

20 pp

QUESTIONS PRESENTED FOR REVIEW

1. Did the Seventh Circuit correctly interpret Section 926.021 of the Ohio Revised Code?

2. Did the Seventh Circuit correctly determine that the Trustee may not avoid the lien created by Section 926.021 of the Ohio Revised Code under the narrow avoidance powers created by 11 U.S.C. §§ 545 and 547?

TABLE OF CONTENTS

Page

Questions Presented for Review i

Table of Authorities iii

Statement of the Case 1

Reasons for Denying the Writ 2

Conclusion 7

Appendix A-1

TABLE OF AUTHORITIES

CASES Page

Farrey v. Sanderfoot, 500 U.S. 291 (1991) 4, 5

In re LMS Holding Co., 50 F. 3d 1526 (10th Cir. 1995) 5

In re Loretto Winery Ltd, 898 F. 2d 715 (9th Cir. 1990) 5

In re Walter, 45 F. 3d 1023 (6th Cir. 1955) 5

In re Woods Farmers Cooperative Elevator, 946 F. 2d 1411 (8th Cir. 1991) 5

McKenzie v. Irving Trust Co., 323 U.S. 365 (1945) . . 3

STATUTES

O.R.C. 926.021 . . . . . 2, 3, 4

O.R.C. 926.06 1

O.R.C. 926.10 1

11 U.S.C. § 522(f) 5

11 U.S.C. § 545 . . . . . 2, 4, 5, 6

11 U.S.C. § 547 . . . . . 2, 3, 4, 5, 6

STATEMENT OF THE CASE

In most respects, respondents agree with the trustee's characterization of the facts and case. A few clarifications, however, are in order.

Merchants Grain, Inc. ("MGI") operated grain warehouses in several states, including Ohio, and served farmers from many states, again including farmers located in Ohio. Contrary to the assertions of the Trustee, moreover, MGI offered a myriad of grain marketing alternatives, including bailment grain, delayed price grain, basis contracts, cash sales, and contract grain. The respondent farmers took advantage of each of these alternatives.

Under Ohio Revised Code ("O.R.C.") 926.06, a grain elevator that wishes to act as a licensed handler must comply with certain financial responsibility requirements. In accordance with this obligation, MGI submitted its annual financial statement to the Ohio Department of Agriculture in August 1990. The Department promptly analyzed the statement and determined that MGI did not meet the statutory net worth requirements. *See* O.R.C. 926.06(B). Despite notice of the problem, MGI had not cured the deficiency by November 1990. Because the fall harvest was well underway by that time, the Department conditionally suspended MGI's license. *See* O.R.C. 926.10. MGI thus remained open, operating under strict conditions. Contrary to the Trustee's suggestion, these conditions did not include the requirement that MGI use grain delivered to its Columbus elevator to pay only Ohio farmers. The Trustee also incorrectly suggests that Ohio's statutory lien protects only Ohio farmers. The lien protects all *depositors*, wherever situated, who deposit grain at licensed elevators in Ohio, as the Seventh Circuit correctly found. Petition at 20a.

In view of the conditional suspension, the Department increased its oversight of MGI. In December 1990, MGI failed to honor a check to a federal agency, and as a result the United States Department of Agriculture suspended MGI's federal license. Thereafter MGI voluntarily closed its doors, and the Department suspended MGI's Ohio license on January 7, 1991.

The Department negotiated with MGI to liquidate the grain on hand at the Columbus, Ohio facility and to use the proceeds to pay the facility's depositors. The parties agreed on terms in January 1991. Under the agreement, MGI liquidated the grain and deposited the proceeds into three escrow accounts; all withdrawals required the signatures of the Department and MGI. Depositors were paid from the respective escrow accounts, depending on the type of grain marketing transaction the depositor had used. All payments to depositors were completed by March 1991.

REASONS FOR DENYING THE WRIT

The holding in this case rests on an interpretation of state law. O.R.C. 926.021 permissibly establishes a statutory lien on grain deposits at Ohio licensed grain elevators to secure payment to in-state and out-of-state farmers. So long as the lien properly arises on deposit, as all three of the lower federal courts found and as is in fact true under Ohio law, the Trustee cannot avoid the lien under federal law. *See* 11 U.S.C. §§ 545, 547. Accordingly, because the timing of the attachment of the lien is a matter of state law and state law alone, the writ should be denied.

The Trustee goes to great lengths in arguing that all three lower courts misconstrued various bankruptcy provisions and thereby improperly prevented the Trustee from avoiding Ohio's statutory lien on grain deposits. The

truth is more straightforward. In order for the Trustee to be empowered to avoid a statutory lien, the lien must arise as a result of the debtor's insolvency. The lien created by O.R.C. 926.021 does not.

As the Seventh Circuit (Cummings, Bauer, *Manion*) correctly found, 11 U.S.C. 547 grants the trustee limited avoidance powers to get back money that was transferred to creditors shortly before a bankruptcy filing. Petition at 7a. That authority, however, does not permit the trustee to ignore statutory liens that treat grain-depositing farmers as secured creditors. Thus, "[t]he trustee's ability to employ section 547(b) to avoid the transfers rises or falls on whether the lien created by Ohio statute was both valid under state law and not prohibited under the Code." *Id.* at 10a. *See McKenzie v. Irving Trust Co.*, 323 U.S. 365, 370 (1945) (looking to state law to determine the extent of property interest under lien).

Not only was the Seventh Circuit correct that this determination turns on state law, but it also was correct in concluding that the lien was valid in this instance. Under O.R.C. 926.021(B), a lien is created on agricultural commodity assets. The lien arises on delivery of the grain to the elevator. O.R.C. 926.021(C). In the event of an elevator failure, exclusive power to enforce the lien transfers to the Director of Agriculture who may liquidate the grain and allocate the proceeds in accordance with the statute's terms. O.R.C. 926.021(D). Nothing in these subsections, or in any of the other provisions of the section, supports the Trustee's naked assertion that the lien attaches only to the assets of an insolvent elevator; the lien arises on deposit. Nor has the Trustee cited a single federal or state court that has embraced this interpretation. At all events, this interpretation (right or wrong) rests on state, not federal, law.

No less flawed is the Trustee's contention that the Seventh Circuit erred in determining that 11 U.S.C. 545 does not permit the Trustee to avoid the farmers' statutory lien. Unlike section 547, to be sure, this provision permits the Trustee to avoid "the fixing of a lien," as opposed to granting the Trustee power to avoid "a statutory lien." But the difference is of no help to the Trustee. Once again, the sole question created by the federal statute is one of timing under state law: Does O.R.C. 926.021 create a lien for the amount of the grain "contemporaneously with delivery"? *See* Petition at 18a-19a. If it does, then MGI acquired the grain subject to the lien; if it does not, then the Trustee *might* be able to avoid the fixing of the lien. In this instance, the lien plainly arose under state law on the delivery of the grain, meaning that the lien was not avoidable under section 545. Indeed, as the Seventh Circuit correctly recognized, this state law analysis parallels to a large degree the one conducted in determining whether section 547 applies. Petition at 19a.

Apparently recognizing the impediment to further federal court review of this essentially state law issue, the Trustee tries to create a substantial federal question where there is none. He argues that the lower court's interpretation of the relationship between section 545 and section 547 differs from that of four other courts and therefore is certworthy. While the Seventh Circuit's examined conclusion differs from the assumptions of four other circuits, as the court itself acknowledged, *see* Petition at 17a n.4, this fact alone does not warrant further review of the issue.

As an initial matter, the Seventh Circuit relied on a decision of this Court in reaching its conclusion. In *Farrey v. Sanderfoot*, 500 U.S. 291 (1991), the Court noted that

section 522(f) of the Code, like section 545, focuses on the "fixing of liens," not the avoidance of liens. And it gave this textual distinction meaning by concluding that the trustee (the debtor, really) must have "had the property interest to which the lien attached at some point *before* the lien attached to that interest" in order to have any avoidance power. 500 U.S. at 296. In this instance, because the debtor (MGI) did not have a property interest in the grain before the statutory lien attached under state law, the trustee lacked avoidance authority under section 545 and therefore authority to get the money back under section 547.

Nor does this conclusion create the kind of lower-court conflict that warrants certiorari. In addition to being supported by *Farrey*, not one of the four lower-court decisions took the time to analyze the interrelation of section 545 and 547. And, from all that appears in the decisions themselves, no party took the time to analyze the relationship either. All you have, in other words, are the unexamined assumptions of four courts that section 545 permits the avoidance of liens as opposed to the avoidance of the fixing of liens.

These assumptions are *dicta* as well, because in each instance the courts rejected the lien avoidance argument when all was said and done. In *In re Walter*, 45 F. 3d 1023 (6th Cir. 1955), the court held that the Trustee could not avoid a tax lien that attached to the debtor's tractor. In *In re LMS Holding Co.*, 50 F. 3d 1526 (10th Cir. 1995), the court held that the debtor in possession could not avoid a tax lien. And in *In re Loretto Winery Ltd.*, 898 F. 2d 715 (9th Cir. 1990), and *In re Woods Farmers Cooperative Elevator Company*, 946 F. 2d 1411 (8th Cir. 1991), the courts refused to allow the Trustees to avoid statutory liens on grapes and on grain respectively. Thus, even giving the Trustee the benefit of the doubt on its assertions of a split, it makes sense to let the

issue percolate in the lower courts to determine whether other courts reject or, as seems more likely, adopt the well-reasoned analysis of the Seventh Circuit on the relationship between sections 545 and 547. That is particularly true here because under Ohio law it remains exceedingly unlikely that the adoption of the Trustee's analysis would make a difference in this case. For even if section 545 permitted the avoidance of a lien, as opposed to the fixing of a lien, the lien was still valid under state law and therefore insulated from the Trustee's avoidance powers.

Finally, the Trustee complains that the Seventh Circuit's opinion "states" that "property subject to a lien is not property of the estate." Petition at 20. No citation is offered to back up this interpretation of the opinion. And none would seem to be able to do so -- particularly if the Trustee means to challenge a holding in the case. All the Seventh Circuit was saying was this: The trustee's ability to avoid the transfers "rises and falls" on whether the Ohio statutory lien was valid. *Id.* at 10a. That conclusion is correct and simply does not warrant further review.

CONCLUSION

For the foregoing reasons, the Court should deny the writ.

Respectfully submitted,

BETTY D. MONTGOMERY
Attorney General
JEFFREY S. SUTTON
State Solicitor
Counsel of Record
SIMON B. KARAS
CHERYL D. MINSTERMAN
Assistant Attorneys General
30 East Broad Street
17th Floor
Columbus, Ohio 43215-3428
(614) 466-8980

WILLIAM B. LOGAN, JR.
Luper, Sheriff & Neidenthal
Special Counsel
50 West Broad Street
Suite 1200
Columbus, Ohio 43215-3384
(614) 221-7663

Counsel for Intervening Respondents The Agricultural Commodity Depositors Fund and The Commodity Advisory Commission

APPENDIX

[§ 926.02.1] § 926.021 Liens on agricultural commodity assets of failed handler; priority.

(A) As used in this section:

(1) "Claimant" means a person who is unable to secure satisfaction of financial obligations due from an agricultural commodity handler.

(2) "Failure" means any of the following involving an agricultural commodity handler:

(a) An inability to financially satisfy claimants;

(b) A public declaration of insolvency;

(c) A revocation of license with outstanding indebtedness to claimants;

(d) Nonpayment in the ordinary course of business where a good faith dispute does not exist;

(e) No application for license renewal;

(f) Denial of license renewal;

(g) Voluntarily surrendering a license.

(3) "Agricultural commodity assets" involving a failed agricultural commodity handler mean any of the following:

(a) All agricultural commodities owned or stored, including agricultural commodities in transit shipped by the failed handler but not yet paid for;

(b) Redeposited agricultural commodities;

(c) Proceeds from the sale of agricultural commodities due or to become due;

(d) The equity less any secured financing directly associated therewith in assets in hedging or speculative margin accounts held by commodity or security exchanges or dealers representing the exchanges, and any moneys due or to become due less any secured financing directly associated therewith from any transactions on the exchanges;

(e) Any other unencumbered funds, property, or equity in funds or property, wherever located, that can be directly traced to the sale of agricultural commodities by the failed handler, provided both that the funds, property, or equity in funds or property shall not be considered to be encumbered unless the encumbrance results from good and valuable considerations advanced by any secured party on a good faith basis and that the encumbrance is not the result of the taking of funds, property, or equity in funds or property as additional collateral for an antecedent debt;

(f) Any other unencumbered funds, property, or equity in assets.

(B) A lien shall exist on all agricultural commodity assets of a failed agricultural commodity handler in favor of any of the following:

(1) Claimants, including lenders, who possess receipts covering grain owned or stored by the handler;

(2) Claimants who possess written evidence of ownership other than a receipt disclosing a storage obligation of the handler, including tickets;

(3) Claimants who surrendered receipts as part of an agricultural commodity sales transaction but were not fully paid for the agricultural commodity and the handler failed within twenty days after the surrender;

(4) Claimants who possess any other written evidence of the sale of agricultural commodities to the failed handler for which they were not fully paid.

(C) The lien which shall secure all claims described in division (D) of this section, shall arise at the time of the delivery of the agricultural commodity for sale, commencement of the storage obligation, or when funds are advanced by the lender, and shall terminate when the liability of the agricultural commodity handler to the claimant is discharged, provided that the priority of each lien among the respective claimants shall not relate to the date the claim arises but shall be governed by the priorities established in division (D) of this section. The lien claims of all claimants shall be considered to be assigned by operation of this section to the department of agriculture, and in the event of a failure and subsequent liquidation, the lien shall transfer over to assets or proceeds of assets either received or liquidated by the department of agriculture.

(D) In the event of a failure, the director of agriculture shall enforce the lien claims and allocate the proceeds as follows:

(1) First priority against all agricultural commodity assets shall be the following:

(a) Claimants, including lenders, who possess receipts covering grain owned or stored by the agricultural commodity handler;

(b) Claimants who possess written evidence of ownership other than receipts disclosing a storage obligation of the handler, including tickets;

(c) Claimants who surrendered receipts as part of an agricultural commodity transaction but were not fully paid for the agricultural commodity and the handler failed within twenty-one days after the surrender.

(2) Second priority against all agricultural commodity assets shall be to claimants who possess written evidence of the sale of an agricultural commodity, including but not limited to tickets, delayed price agreements, or similar agricultural commodity delivery contracts who completed delivery and pricing within thirty days immediately prior to the failure of the handler.

(3) To the extent not necessary to satisfy first and second priority claimants, all other claimants who possess written evidence of the sale of agricultural commodities to the failed handler shall participate in the pro rata distribution of the remainder of the agricultural commodity assets in an amount not to exceed the value of their claim.

(E) In the event that any adversary proceeding is commenced to recover agricultural commodity assets upon which the lien imposed in this section is imposed and the department of agriculture declines to enter the proceeding, the director of agriculture, upon application to him by any claimant, shall assign to the claimant the applicable lien to permit the claimant to pursue his lien in the adversary proceeding to the extent the action will not delay the resolution of the proceeding, the prompt liquidation of the assets, or the ultimate distribution of the assets of all claimants.

§ 926.06 Issuance of licenses.

(A) The director of agriculture may issue a handler's license, or renewal thereof, upon the payment of the prescribed application fee, if the director is satisfied that the applicant meets the standards of financial responsibility required under this section and has complied with this chapter and the rules adopted under it.

(B) Each applicant for a handler's license, or renewal thereof, shall have and maintain current assets equal to or greater than current liabilities and a total net worth of at least ten cents per bushel for the total number of bushels of agricultural commodities that he handled during the immediately preceding twelve-month period to cover any indebtedness arising from his operations as a licensed handler. If an applicant is applying for a handler's license for the first time and did not handle any agricultural commodities during the immediately preceding twelve-month period, he shall have an allowable total net worth of at least twenty-five thousand dollars for that purpose. No person shall be licensed as a handler unless he has an allowable total net worth of at least twenty-five thousand dollars. Any deficiency in required total net worth may be compensated for by an indemnity agreement executed by a person pledging personal assets for the benefit of commodity creditors should the licensed handler default in his obligations to the creditors; a bond issued by a corporate surety company that is authorized to do business under the laws of this state; or, at the director's discretion, an irrevocable letter of credit issued by a bank or other lending institution that is authorized by this state or the United States to issue such letters of credit and is subject to service of process in this state for any suit on the bond or letter of credit. A bond shall be made to the treasurer of the state of Ohio to be deposited in the

agricultural commodity depositors fund created under section 926.16 of the Revised Code for the benefit of any person who may be injured by the handler's failure to meet obligations arising under this chapter. A letter of credit shall be issued for the benefit of the department of agriculture and the agricultural commodity depositors fund.

In determining total net worth, credit may be given for fixed assets such as buildings, machinery, and equipment, in the amount of the insured value of such assets under a policy of insurance against loss or damage or, at the discretion of the director, in the amount of their current market value as determined by an accredited rural appraiser or an appraiser certified by the American appraisal institute. The appraiser shall be completely independent of any relationship with the handler. Capital stock shall not be considered a liability for the purpose of determining total net worth. Regardless of the total number of bushels of agricultural commodities that he handled during the immediately preceding twelve-month period, an applicant's total net worth need not exceed three hundred thousand dollars.

(C) In order for the director to determine if an applicant meets the standards of financial responsibility required under division (B) of this section, the applicant for a handler's license, or renewal of a handler's license, shall submit a current financial statement prepared by a qualified person who is not directly associated with the applicant's business. The financial statement shall consist of a balance sheet showing the current and deferred assets and liabilities of the applicant, a statement of income, a statement of retained earnings, a statement of changes in financial position, and whatever notes are sufficient to explain the details contained in the financial statement.

The financial statement accompanying an applicant's original application shall show a statement closing date that is within six months of the date of application. Thereafter, the applicant applying for renewal shall submit an annual statement not later than ninety days after the close of his business year.

The director may require an applicant for a handler's license, or renewal of a handler's license, to submit a financial statement prepared by a certified public accountant licensed under the laws of this state, and may require the attachment to the statement of the accountant's opinion of the applicant's financial status based on his examination of the records conducted in accordance with generally accepted auditing standards if the director determines that the first financial statement submitted under this division is incomplete or otherwise unsatisfactory.

(D) The director may prepare and publish statistical abstracts of information obtained under this section without disclosing details that would identify a particular applicant with particular statistics. Such information is otherwise confidential for purposes of section 102.03 of the Revised Code, and records of the department of agriculture containing such information are not otherwise public records under section 149.43 of the Revised Code.

§ 926.10 Suspension or refusal of license.

The director of agriculture may by order refuse to grant or may suspend or conditionally suspend a handler's license, without prior hearing, when he determines that there is reasonable cause to believe that the applicant or licensee:

(A) Has failed to maintain the insurance coverage required under section 926.07 of the Revised Code;

(B) Has failed to maintain accurate and complete records and accounts as required under section 926.11 of the Revised Code;

(C) Has failed to charge, collect, or remit the fee required under division (B) of section 926.16 of the Revised Code;

(D) Has refused to allow the director or his authorized representative to examine, at a reasonable time, his accounting records, accounts, agricultural commodity inventories, or warehouse;

(E) Does not have in his possession sufficient agricultural commodities to cover the outstanding receipts or tickets issued or assumed by him under bailment agreements;

(F) Has issued a receipt in violation of this chapter or any rules adopted under it;

(G) Does not have the net assets specified in division (B) of section 926.06 of the Revised Code or has failed to obtain a bond or other protection for any deficiency in required net assets as provided in that division;

(H) Does not have his obligations for agricultural commodities purchased under delayed price agreements secured or represented as required under division (B) or (C) of section 926.29 of the Revised Code.

The applicant or licensee to whom a denial or suspension or conditional suspension order is issued shall be afforded a hearing in accordance with Chapter 119. of the

Revised Code, after which the director shall issue or deny the license applied for in the pending application or reinstate or revoke the suspended or conditionally suspended license. The director may suspend or conditionally suspend or revoke a license after a hearing held in accordance with Chapter 119. of the Revised Code for any other violations of this chapter or any rules adopted under it.

The director shall cause a notice to be posted on the property of a person whose license has been suspended, conditionally suspended, or revoked stating the limitations or restrictions imposed on the person in the handling of agricultural commodities as a result of the suspension, conditional suspension, or revocation. The notice shall not be removed from the property without written authorization from the director.

Supreme Court, U.S.
FILED
JAN 16 1997
CLERK

No. 96-831

IN THE
Supreme Court of the United States
OCTOBER TERM, 1996

EDMUND M. MAHERN, TRUSTEE FOR MERCHANTS GRAIN, INC.,
Petitioner,

v.

MARK AND CHRIS ADKINS, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

REPLY BRIEF OF PETITIONER

JAMES M. CARR
JOSEPH H. YEAGER, JR.
BAKER & DANIELS
300 North Meridian Street
Suite 2700
Indianapolis, IN 46204
(317) 237-0300
Counsel for Petitioner

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

IN THE

Supreme Court of the United States

OCTOBER TERM, 1996

No. 96-831

EDMUND M. MAHERN, TRUSTEE FOR MERCHANTS GRAIN, INC.,
Petitioner,

v.

MARK AND CHRIS ADKINS, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

---

REPLY BRIEF OF PETITIONER

Respondents-Intervenors the Ohio Agricultural Commodity Depositors Fund and the Ohio Commodity Advisory Commission (collectively, "the Fund") conclude their brief in opposition by writing: "The trustee's ability to avoid the transfers 'rises and falls' on whether the Ohio statutory lien was valid. [Petition] at 10a." Brief in Opposition at 6.

That characterization is wrong. It ignores the federal-law half of the Seventh Circuit's analysis—precisely the half upon which this case now turns. In fact, the Seventh Circuit actually wrote, in the passage from which the Fund quotes, that the Petitioner's ability to avoid the transfers "rises or falls on whether the lien created by the Ohio statute was *both* valid under state law *and not prohibited under the Code*." Petition at 10a, emphasis supplied. The Fund omits from its quote (and, largely, from its brief)

reference to the critical second element—avoidability under federal law. However, it is that federal issue that the Seventh Circuit decided erroneously and that deserves this Court's attention.

This fundamental misapprehension aside, the Brief in Opposition also unfairly attempts to diminish the importance of the federal issue by suggesting that the fully-formed conflict among the circuits be allowed to "percolate," and seeks to play down the split among five circuits on this issue that the Seventh Circuit itself acknowledged.[1]

I. THE FUND WRONGLY ARGUES THAT THE STATE LAW VALIDITY OF ITS LIEN DETERMINES THE OUTCOME OF THIS CASE.

Rather than address them, the Fund asks the Court to overlook the important issues of federal law that lie at the heart of the decision below.

The Fund takes no issue with Petitioner's explanation in his Petition that Bankruptcy Code § 545 is the product of over 50 years of federal legislation aimed at balancing the rights of states to regulate their own commercial affairs against the need for uniformity and fair and equal distribution among the citizens of various states in multi-state bankruptcies. Neither does the Fund seek to reconcile the differences between Bankruptcy Code § 545 and Bankruptcy Code § 522 that make *Farrey v. Sanderfoot*, 500 U.S. 291 (1991), a § 522 case, inapplicable to § 545. Instead, the Fund concentrates on a state law issue that is not part of the Petition—the Seventh Circuit's interpretation of the Ohio lien statute (an interpretation not attacked in the Petition). On this, the Fund concludes:

> For even if section 545 permitted the avoidance of a lien, as opposed to the fixing of a lien, the lien

---

[1] The Fund also wrongly disputes that the Ohio Department of Agriculture required MGI's Ohio grain be used to pay only Ohio creditors. Brief in Opposition at 1. In fact, the Bankruptcy Court so found. Petition at 40a, note 26.

was still valid under state law and therefore insulated from the Trustee's avoiding powers.

Brief in Opposition at 6.

The Fund's position ignores the Bankruptcy Code. A lien valid under state law may still be avoided if it falls within one of the categories of liens avoidable under the Bankruptcy Code, including the four categories described by § 545. In suggesting that the analysis begins and ends with state law, the Fund's argument proves too much by writing § 545 out of the Code.

The Seventh Circuit did not ignore this issue. Instead, it directly addressed § 545, relying on a new interpretation of that section to detour around the Trustee's right to avoid the liens in question under § 545(2). Were the Fund's analysis correct, the Seventh Circuit could have written a much shorter opinion, concluding that the lien's validity under state law ended the debate.

II. THE ISSUES ARE IMPORTANT ENOUGH TO MERIT REVIEW BY THIS COURT.

Proper and prompt resolution of these federal issues is important. If the Seventh Circuit decision stands, it will encourage state legislatures to model statutes after the Ohio statute in an attempt to give their own citizens a bankruptcy priority over creditors residing in other states.[2] That piecemeal result is just what the framers sought to avoid by giving Congress the express power to make uniform national bankruptcy law and what Congress sought to avoid by adopting § 545. Wide adoption of the Seventh Circuit's approach would directly undermine the uniformity of national bankruptcy distribution.

---

[2] The Fund implies that because the Ohio statute would theoretically apply also to non-Ohio farmers selling grain in the State, no improper priority is created. Brief in Opposition at 1. This implication is false. The mere fact that some citizens from other states may incidentally benefit from the state-created priority does nothing to change the fact that it is a state-created priority that works in derogation of the uniform scheme of distribution created by the Bankruptcy Code.

The Fund argues that this Court should let the issue "percolate." Brief in Opposition at 6. However, this case does not call for percolation. The issue here is not a fact-sensitive problem that treatment by more courts under varied fact patterns will better define—as, for instance, in a Fourth Amendment case that may depend heavily on the facts of a challenged search. Instead, the issue is well-defined already. No amount of waiting will sharpen it. Moreover, guidance provided now will avoid years of uncertainty (and likely incorrect decisions, at least in the lower courts of the Seventh Circuit following Circuit law).

III. CONTRARY TO THE FUND'S SUGGESTION, THE CIRCUITS ARE NOW SPLIT ON WHETHER A STATE CAN DODGE § 545 BY A RELATION-BACK CLAUSE.

The Fund does acknowledge the Seventh Circuit's statement that its decision on the issue departs from that of the parties, the courts below in this case, and at least four *prior* decisions of other circuits. Brief in Opposition at 4-5. The Fund does not come to grips with the fact that every other Court publishing an opinion on point has applied § 545 in a manner precisely opposite to that now applied by the Seventh Circuit. This Court should measure conflict not by speculating about how another circuit may have decided a case under different law, but instead based on the way the circuits have actually interpreted and applied the statute in question. On that, the Seventh Circuit was right—its holding does digress from everything that has gone before. Petition at 17a.

The Seventh Circuit was not as sanguine in making this holding as the Fund is now in defending the decision. The Seventh Circuit readily acknowledged its disagreement with "[t]he Trustee, the farmers, both courts below, and many other court decisions." Petition at 17a. The Seventh Circuit admitted—indeed highlighted—the con-

flict among the circuits that its holding created.[3] If the Seventh Circuit was on the right track when it refused to apply § 545 to this case, then all the parties to this case, all the courts below, and at least four other circuits have been wrong on that same issue.

CONCLUSION

As the Trustee demonstrates in his Petition, this Court should grant certiorari to correct the Seventh Circuit's evisceration of the Congress' carefully constructed scheme of uniform and equal national distribution. The Seventh Circuit's holding allows a state to circumvent Bankruptcy Code § 545, and the universally-recognized federal goal of uniform and equal national bankruptcy distribution that lies behind it, by the simple expedient of writing a state priority statute that, even though enforceable only against assets of "failed" (insolvent) companies, bears a relation-back clause reciting that the lien granted "arises" on delivery of the commodity in question. This erroneous application of *Farrey v, Sanderfoot* to § 545 should be reversed now, before it has a chance to take root and undermine years of legislation, affect thousands of bankruptcy cases and misdirect millions of dollars in bankruptcy distributions.

Respectfully submitted,

JAMES M. CARR
JOSEPH H. YEAGER, JR.
BAKER & DANIELS
300 North Meridian Street
Suite 2700
Indianapolis, IN 46204
(317) 237-0300
Counsel for Petitioner

January 16, 1997

[3] The Fund itself acknowledged below that § 545 worked to avoid liens, not the "fixing" of liens. For example, in its brief to the Seventh Circuit, the Fund noted "Section 545 provides four situations where a trustee may avoid a statutory lien." Brief of Appellees at 28.